Understanding Chronic Illness and Long-Term Care Life Insurance Options

Disclosures

As personal situations change, so will an individual's life insurance needs. Care should be taken to ensure this product is acceptable for long-term life insurance needs. Any associated costs should be considered before making a purchase. Life insurance has fees and charges that include costs of insurance which vary based on gender, health, and age, and has additional charge for riders.

A fixed annuity is a long-term, tax-deferred insurance contract designed to create a fixed stream of income through a process called annuitization while providing a fixed rate of return. Withdrawals from fixed annuities may be subject to surrender charges and ordinary income taxes. If a withdrawal is made prior to age 59 ½, an additional 10% tax penalty may apply.

Products issued and underwritten by The State Life Insurance Company® (State Life), Indianapolis, IN, a OneAmerica company that offers the Care Solutions product suite.

Any individuals used in scenarios are fictitious and all numeric examples are hypothetical and were used for explanatory purposes only.

Disclosures Continued

Riders are optional and carry an additional cost. The long-term advantage of an optional benefit will vary with the terms of the benefit option and the length of time the product is owned. As a result, in some circumstances, the cost of an option may exceed the actual benefit paid under the option.

Please note that the replacement of an existing annuity must not be made unless all factors are weighed and it is documented as suitable for the client.

Policy form series *Asset-Care*: L301, SA31, R501, L301 (FL), SA31 (FL) 1, R501 (FL), R509 (FL); *Annuity Care*: SA34, R508, SA34 (FL) 1, R504 (FL) TQ, R505 (FL), R505 (FL) TQ, SA34 (TX)-R; Annuity Care II: SA35, SA35 (ID), SA35 (FL) 1, R521 (FL), R522 (FL), SA35 (TX); *Indexed Annuity Care*: SA36, ICC14 SA36, R529, R529 PPA, ICC14 R529 PPA, ICC14 R529 R530, R530 PPA, ICC14 R530 PPA, ICC14 R530.

All guaranteed are subject to the claims paying ability of State Life.

All numeric examples are hypothetical and were used for explanatory purposes only. Provided content is for overview and informational purposes only and is not intended as tax, legal, fiduciary, or investment advice.

7702B vs. 101g Policies

With the aging of America, preparing for long-term care is becoming more important than ever.

In the past, the only way to cover this risk was with traditional long-term care insurance.

The good news is that today's marketplace provides more options.

7702B vs. 101g Policies

A growing number of products can combine some of the favorable qualities of life insurance and benefits for end of life care in one package.

These approaches help overcome the common “use it or lose it” objection to traditional long-term care insurance by providing benefits even if care is never needed.

In addition, some products provide benefit and premium guarantees that traditional long-term care insurance cannot.

Two Very Different Approaches

When examining these products, it is important to understand there are two very different approaches that can determine what type of claims qualify for benefits, how those benefits are paid out, and how any applicable costs are applied.

Understanding these differences is important so agents can present their clients an accurate picture of what is being purchased.

Two Very Different Approaches

1. Life insurance with accelerated death benefit for chronic illness riders (101g)

2. Life insurance with long-term care benefits (7702B)
    - Life insurance with long-term care riders
    - Asset-Based long term care

Accelerated Death Benefit for Chronic Illness Riders - 101g

According to section 101g of the Internal Revenue Code, any amount received under a life insurance contract on the life of an insured who is chronically ill shall be treated as an amount paid by reason of the death of the insured.

These policies always pay benefits on an indemnity basis. Is that an advantage?

- Bill administration
- Ability to pay family members

Life Insurance with Long-Term Care Benefits - 7702B

Life insurance products with long-term care benefits and/or riders fall under the classification of IRC Code Section 7702B and typically offer more comprehensive coverage. These policies usually pay benefits on a reimbursement basis.

All versions of Asset-Care are 7702B long-term care policies.

Summary of Typical Differences

Marketing Guidelines

Access to Death Benefit

Temporary vs. Permanent Conditions

Tax Treatment of Benefits

Continuation of Benefits Rider

Claims Qualifications

Marketing Guidelines

Policies with an accelerated death benefit for chronic illness (101g), cannot use the term "long-term care" in marketing or sales literature.

On the other hand, life insurance policies that qualify under IRC Code 7702B can be marketed as "long term care benefits."

Examples of 101g Rider Names

Accelerated Access Solution

LifeEnhance Accelerated Benefits Rider

Enhanced Care Benefit

Premier Living Benefits Rider

ExtendCare

Accelerated DB for Chronic Illness

Example of 101g Rider

Accelerated Death Benefit Plus Rider	This rider advances a portion of the death benefit in the event of a named Specified Medical Conditions, Permanent Confinement to a Nursing Home, or Terminal Illness as defined in the rider. If the rider benefit is exercised, interest charges will be assessed. Other charges may apply. This rider will be automatically included with Your policy if approved in Your state, subject to the underwriting classification of the insured. (CLR-143 1308 OH)
Accelerated Death Benefit Life Plus Rider	This rider advances a portion of the death benefit for Terminal Illness, certain Specified Medical Conditions or Chronic Illness. Chronic Illness is defined as being unable to perform two of the six Activities of Daily Living (ADL) for at least 90 days. If the rider benefit is exercised, interest charges will be assessed. Other charges may also apply. This rider will be automatically included with Your policy if approved in Your state, subject to the underwriting classification of the insured. (CLR-202 1409 OH)

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Access to Death Benefit – 101g

Chronic illness riders can be paid for with an internal cost of insurance charge, or may be available at no charge in conjunction with a discounted acceleration of the death benefit (known as Actuarial Discounting).

The insurance company will use factors such as age, gender, and interest rates to determine what portion of the death benefit will be available – at the time of claim.

Example of Actuarial Discounting

	Life Insurance with Long-Term Care Benefits	Life Insurance with Chronic Illness Rider (Using present value discounting method)
Death Benefit	$300,000	$300,000
Maximum benefit payout	2% per month	Present Value of 24% of the Death Benefit
Year 1	$72,000 (Death Benefit is reduced to $228,000)	$36,000 (Death Benefit is reduced to $228,000)
Year 2	$72,000 (Death Benefit is reduced to $156,000)	$36,000 (Death Benefit is reduced to $156,000)
Year 3	$72,000 (Death Benefit is reduced to $84,000)	$36,000 (Death Benefit is reduced to $84,000)

For illustration and training purposes. All numeric examples are hypothetical, and are for explanatory purposes only.

Access to Death Benefit - 7702B

These policies typically make up to 100% of the death benefit available for long-term care, subject to monthly limits.

Long-term care benefits are determined up front at the time of policy issue.

Because of the significant differences between 101g and 7702B policies, it is crucial that the client understand how benefits are calculated and paid.

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Temporary vs. Permanent Conditions - 101g

Chronic illness riders can vary widely. To qualify for a claim, a licensed healthcare provider must certify a chronic illness.

Most policies only pay benefits when the illness "is likely to last the rest of the insured's life."

Temporary vs. Permanent Conditions - 7702B

To qualify for claim, the client must meet the basic definition of chronic illness, which requires a licensed healthcare provider to certify the insured, for a period of at least 90 days, is unable to perform two of six Activities of Daily Living (ADLs) or is cognitively impaired.

These policies pay benefits for both temporary and permanent conditions.

Temporary vs. Permanent Conditions

Certain health conditions will allow the insured to receive benefits under both 101g and 7702B policies.

These would be permanent and non-recoverable conditions such as:

- Cognitive impairment (Alzheimer’s disease, Dementia, etc.)
- ALS (Lou Gherig’s disease)
- Parkinson’s disease

Temporary vs. Permanent Conditions

With other medical conditions, such as strokes, a 7702B policy likely has significant advantages over a policy with a chronic illness rider.

Only 25% of stroke victims die shortly after the stroke or need permanent care in a Nursing Home or other LTC facility.

Source: The New Jersey Comprehensive Stroke Center at University Hospital, “Stroke Rehabilitation”, 2013

Temporary vs. Permanent Conditions

10% of stroke victims recover almost completely

25% recover with minor impairments

40% experience moderate to severe impairments that require some care

In many cases these impairments would not be expected to be permanent, so benefits would not be payable under a chronic illness (101g) rider.

Source: The New Jersey Comprehensive Stroke Center at University Hospital, “Stroke Rehabilitation”, 2013

Temporary vs. Permanent Conditions

Injuries sustained as a result of accidents may also be treated differently depending on the type of contract.

People age 75 and older who fall are four to five times more likely than those age 65 to 74 to be admitted to a long-term care facility for a year or longer.

Even if assistance was needed with 2 of 6 ADLs, benefits would not be payable under a chronic illness rider unless the condition was considered permanent.

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Tax Treatment of Benefits – 7702B

LTC benefits paid from Code Section 7702B policies are generally treated as excludable accident and health insurance benefits under Code Section 104(a)(3), and are therefore income tax free.

Tax Treatment of Benefits – 101g

Benefits paid as an acceleration of death benefit from Code Section 101g policies generally are excludable from income like death benefits. However, they may be taxable if the IRS per diem limit ($340 in 2016) is exceeded. The per diem limit can change on an annual basis, but it remained the same from 2014 to 2015.

The tax treatment will depend on a number of specific factors, and the policy owner should consult with their CPA regarding tax treatment of benefits.

Tax Treatment of Benefits – 101g

Many 101g policies will not pay benefits in excess of the IRS per diem limit at the time of policy issue, so the stated monthly benefit may be misleading.

If the policy allows for distributions in excess of the IRS per diem limit there could potentially be significant tax consequences which must be explained to the client.

Supplemental Illustration
Accelerated Death Benefit Life Plus Rider Values Report
Non-Guaranteed Values

Age	End of Year	Cash Surrender Value	Net Amount at Risk	Death Benefit	Chronic Illness Max Periodic Payment Advance [1,2]	Chronic Illness Max Lump Sum Advance Amount	Chronic Lump Sum Remaining Death Benefit
78	16	515,445	24,728	541,217	262,076	514,497	15,881
79	17	554,621	26,608	582,352	282,000	553,601	17,088
80	18	596,705	28,627	626,540	303,404	595,607	18,384
81	19	641,900	30,796	673,995	326,391	640,719	19,777
82	20	690,420	33,124	724,941	351,072	689,151	21,271
83	21	742,495	35,623	779,619	377,561	741,129	22,875
84	22	798,362	38,303	838,280	405,981	796,894	24,597
85	23	858,275	41,179	901,189	436,461	$\boxed{856,698}$	26,442
86	24	922,499	44,261	968,624	469,137	920,804	28,420
87	25	991,323	47,564	1,040,889	504,155	989,501	30,541

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Continuation of Benefits Rider

Most chronic illness riders allow the insured to access a percentage of the policy's death benefit per month (usually 1-4%) up to the full face amount, or a fraction thereof.

Unfortunately this means that the total amount of coverage is limited, as is the benefit duration.

Continuation of Benefits Rider

Some 7702B policies, including Asset-Care, offer the option to purchase additional LTC benefits above and beyond the death benefit.

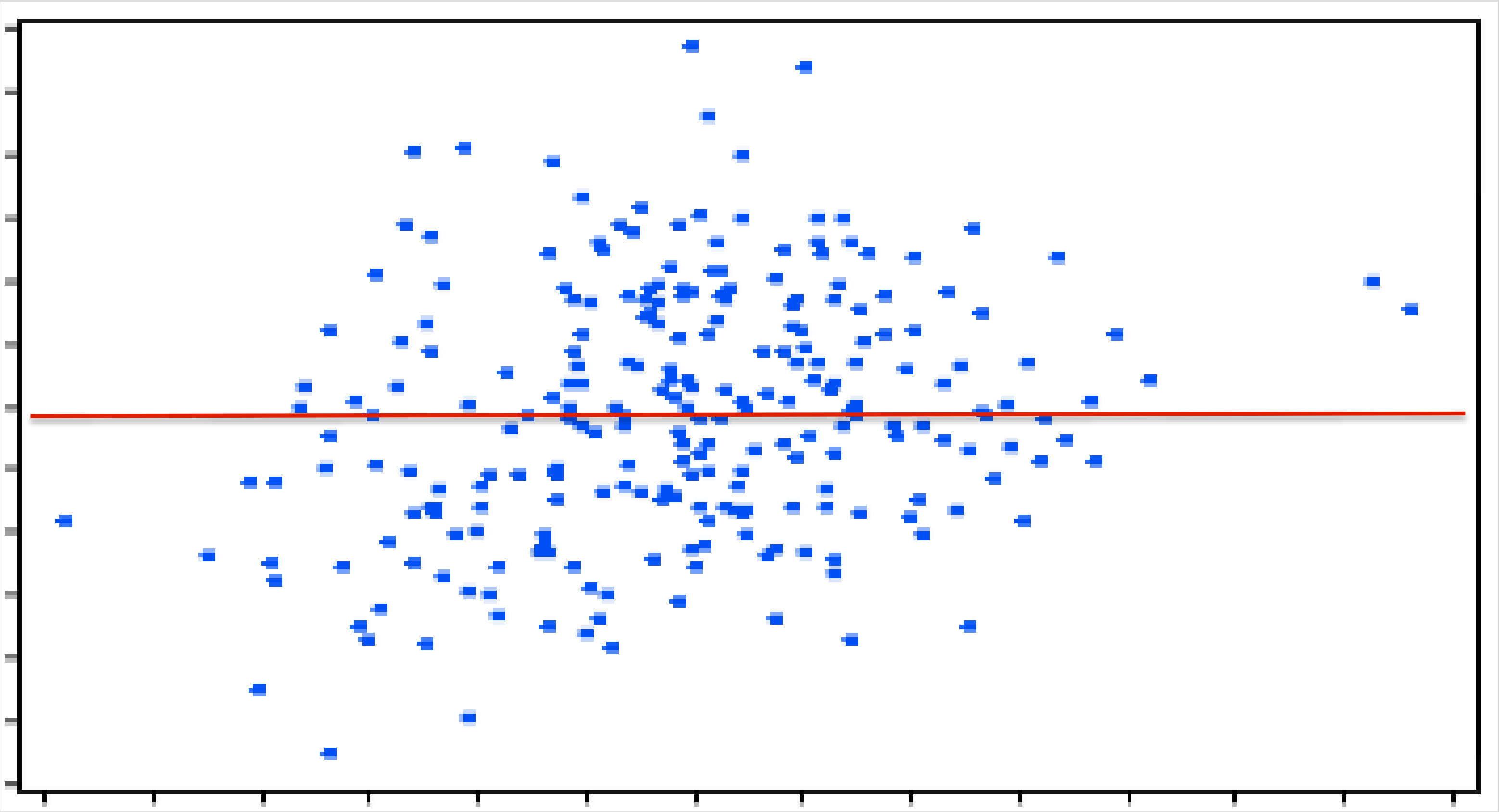
On Asset-Care this feature is called the Continuation of Benefits rider.

Continuation of Benefits Rider

Asset-Care is unique because it is the only policy on the market today that offers optional Lifetime benefits.

Is 50 months of coverage enough?

The Problem with Averages



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Claims Qualifications

Claims qualifications on 7702B policies are standardized by law. There are two ways to qualify:

- Being unable to perform at least 2 of 6 activities of daily living
- Requiring care as a result of cognitive impairment (such as Alzheimer's disease)

Claims Qualifications

Claims qualifications on 101g policies are not standardized by law. They can be similar to 7702B policies, but often are significantly different. Here are a few examples:

> “Requiring continuous confinement in a LTC Facility or under a written plan of Home Care, and stay for rest of life.”
>
> “Confined to a nursing home for 6 months or terminally ill with a 6 month life expectancy”

Claims Qualifications

The elimination period on 7702B policies is generally 90 days, but it can be shorter.

Asset-Care, for example, has a 30 day elimination period for Home Health Care, and a 60 day elimination period for all other services.

Claims Qualifications

The elimination period on life insurance policies with chronic illness riders is usually 90 days, but they can vary widely. Here are a few examples:

"12 months in a Nursing Care Facility"

"2 years"

"6 months (Nursing Home Usage Only)"

Example #1:
101g Policy vs. Asset-Care

Other Company (individual policies)			
	Male - 65	Female - 65	TOTAL
Premium	$100,000	$100,000	$200,000
Death Benefit	$221,487	$268,000	
Example Claim:	**5 years**	**7 years**	
Maximum Acceleration - 80%	**$177,189**	**$214,400**	
Actuarial Discount (4.5% / year)	**$39,867**	**$67,536**	
Acceleration Amount	**$137,322**	**$146,864**	
Cash Surrender Value			
Year 5	$36,424	$36,591	$73,015
Year 15	$0	$0	$0
Year 25	$0	$0	$0

OneAmerica "Asset Care" (joint policy)		
	Male - 65	Female - 65
Premium (Base Policy + Rider)	$200,000	
Death Benefit	$246,891	
Example Claim:	**5 years**	**7 years**
Monthly LTC Benefit	**$7,406**	**$7,406**
LTC Payout Duration	**Lifetime**	**Lifetime**
LTC Benefits Paid	**444,360**	**622,104**
Cash Surrender Value		
Year 5	$145,075	
Year 15	$167,501	
Year 25	$202,737	

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Example #2:

7702B Policy vs. Asset-Care

Life Insurance with LTC Rider	
	Female - 54
Premium	$100,000
Death Benefit	$256,818
Monthly LTC Benefit (2%)	**$5,136**
LTC Payout Duration	**50 months**
Example Claims:	
2 years	$123,264
4 years	$246,528
6 years	$256,800

OneAmerica "Asset Care"	
	Female - 54
Premium	$100,000
(Base Policy + Rider)	
Death Benefit	$167,429
Monthly LTC Benefit (2%)	**$6,697**
LTC Payout Duration	**Lifetime**
Example Claims:	
2 years	$160,728
4 years	$321,456
6 years	$482,184

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Example #3:
7702B Asset-Based LTC Policy vs. Asset-Care

7702B Policies with C.O.B. Rider (individual policies)		
	Male - 67	Female - 64
Premium	$100,000	$100,000
Guaranteed Death Benefit	$117,743	$140,520
Monthly LTC Benefit	$4,906	$5,855
LTC payout duration	6 years	6 years
Example Claims:		
3 years	$176,616	$210,780
5 years	$294,360	$351,300
7 years	$353,232	$421,560

OneAmerica "Asset Care" (joint policy)		
	Male - 67	Female - 64
Premium	$200,000	
(Base Policy + Rider)		
Guaranteed Death Benefit	$297,384	
Monthly LTC Benefit	$5,947	$5,947
LTC payout duration	Lifetime	Lifetime
Example Claims:		
3 years	$214,092	$214,092
5 years	$356,820	$356,820
7 years	$499,548	$499,548

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Conclusion

As you can see, life insurance policies with chronic illness riders are very different from 7702B long-term care policies, and should never be marketed as “long-term care insurance.”

It is also vital that we give our clients an accurate portrayal of exactly what they are purchasing.