

Reading between the lines: A deeper dive into the differences between LTC and chronic illness riders

Vol. 2 in a series on LTC and chronic illness riders

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The differences between long-term care (LTC) riders and chronic illness riders have been a subject of confusion for many advisors and industry professionals wanting to feel more secure in their knowledge and ability to offer solutions that will meet client expectations at claim time. Part one of this series discussed the differences of how each rider is classified and how that effects claims and payment of benefits from the riders. Knowing these differences is extremely important so the insurance professional can present their client with a clear picture of what they are purchasing and what benefits they will receive. To review this information, please request the white paper, *Understanding the variations between long-term care and chronic illness riders – Part I*, NFM-10801AO.

In the past, one of the main differentiators was that a chronic illness rider claim required that the insured to be certified that “care services will likely be needed the rest of the insured’s life” – or in other words – the condition had to be deemed non-recoverable. While there are many other important differences, the non-recoverable requirement was the one easiest to understand, and considered the most important difference by many advisors and clients purchasing coverage. But new regulatory changes may have muddied the waters further.

The Interstate Compact is a group comprised of most but not all states who have agreed to a unified set of standards for approving insurance products. Effective as of December 2014, the Interstate Compact revised standards for chronic illness riders, which receive tax favored treatment as an accelerated life insurance benefit under Internal Revenue Code §101(g). The new standards now allow insurance companies to develop chronic illness riders that include the option of paying temporary chronic illness claims so long as the base regulatory requirement is met that requires the condition to last at least 90 days. These revised standards provide the option to pay temporary claims, but it is not a requirement. At this point, most chronic illness riders still require the claim to be permanent, but there are now a few insurance companies that will pay temporary chronic illness rider claims. Also, note that this change in regulation is not grandfathered back on existing policies. Any policy that was issued under a contract requiring a permanent condition to qualify for claim will still require a permanent condition.

This change in regulation may have blurred the lines even more between chronic illness riders and LTC riders. Some advisors are now under the impression that if the chronic illness rider will pay temporary claims, then it is equivalent to a LTC Rider. But that is not the case. In addition to underwriting and benefit payout differences many chronic illness riders implement (discussed in the Part One white paper referenced above), there is much more differentiating the two products – and these differences center largely on important consumer protections.

Digging deeper — the importance of consumer protections

This purpose of this paper is to focus on important Consumer Protections that further set LTC Riders apart from chronic illness riders and how they can help protect an insured and their LTC benefits even if in some cases when their policy has lapsed.

But first, it might help to preface the discussion with a few statistics.

**Cognitive impairment
is the #1 cause of LTC
claims over age 65¹**

**Deaths from Alzheimer's
has increased 71% since
the year 2000²**

**1 in 3 seniors will die
while having Alzheimer's
of another form of
dementia²**

These statistics help set up the value of consumer protections.

What are “consumer protections”?

LTC Riders on life insurance have mandatory built in features that are required of all traditional LTC policies or riders on any type product sold as “long-term care insurance” coverage. Consumer protection provisions provide important features that protect policy owners from situations that may unintentionally arise due to a physical or cognitive incapacitation, resulting in an individual's LTC coverage being put in jeopardy. These provisions help protect the consumer from an unintended policy lapse, and even possible loss of benefits on an already lapsed policy.

These same consumer protections are not required of chronic illness riders, so without careful reading of the specific terms of the chronic illness contract intended for purchase, one cannot be sure if some or any consumer protections are included with the policy.

The following is a description of consumer protection features that can make a real difference in protecting the ability for claims payments to be received if ever needed. This is not a complete list of LTC consumer protections, but rather, protections that specifically help guard the policy from unintended lapse or protect the insured from loss of benefits in certain situations where a policy has already lapsed.

Unintentional lapse

All LTC policies and LTC riders are required to have this feature.

- The *unintentional* lapse feature requires that the insurance company provide the opportunity for the policy owner to set up an authorized representative (third party contact). If the policy is in danger of lapse, notice must be sent to the policy owner and their authorized representative (if one is assigned) within 30 days of lapse to inform them that the policy is in danger of lapse and premium needs to be paid to keep the policy in force. The opportunity to assign an authorized representative must be offered to the policy owner at policy issue and every two years thereafter..
- This feature does not guarantee the policy will not lapse, but rather is meant to help prevent unintended lapse due to a policy owner's functional incapacity or a cognitive reason that leaves them unable to pay premium.

Chronic Illness riders are not required to offer this feature. The consequences of not having an unintentional lapse

feature on a policy could potentially be further compounded by the following three features that are also not required on a chronic illness rider.

Lapse protection while on claim

All LTC policies and LTC Riders are required to have this feature.

- The lapse protection feature requires that LTC benefits cannot be lapsed while the insured is on claim and receiving LTC benefits. Thus, even if cash values (or values in a shadow account) go to \$0, the insurance company must continue to pay LTC benefits.
- Any remaining death benefit that has not been not accelerated upon the death of the insured is not covered under this provision. How companies treat the remaining death benefit when a policy was kept in force by the lapse protection provision will vary by company. Some companies protect all remaining death benefit, some protect any unpaid amount tied to the LTC specified amount, and some companies do not protect any remaining death benefit for payment to beneficiaries. If the insured goes off LTC claim, the lapse protection on any remaining death benefit ceases unless the insured goes back on LTC claim.

Chronic illness riders are not required to have this feature. A few companies include it, but most do not. In addition, insurance companies can and often do require premiums to be paid to keep the policy in force while the insured is on chronic illness claim.

Reinstatement provision

All LTC policies and LTC riders are required to have this feature.

- The *reinstatement provision* on a LTC policy or LTC rider has more liberal standards than the reinstatement provision of a life insurance policy. Under the reinstatement provision of a LTC policy or LTC rider, reinstatement must be available for a period of time without any evidence of insurability. The reinstatement must be requested within five months of the date of policy termination and reasonable evidence must be shown that the insured either had a functional incapacity or a cognitive reason for being unable to pay the premium due that would have kept the policy in force. As part of the reinstatement procedure, premiums will need to be paid and the policy brought back into good order. Upon reinstatement requirements being met, the policy is considered back in force with all rights and provisions available.
- Interestingly, when a LTC rider is added to a life insurance policy, the strict requirements of the reinstatement provision of the life insurance policy are softened by the more liberal standard required of the LTC rider – which is a positive benefit to the policy owner since both the LTC rider and the base policy must be reinstated without evidence of insurability.

Chronic Illness riders, which are governed by life insurance regulations, are not required to offer the same standards for reinstatement required of a LTC policy or LTC rider. Thus, you will want to carefully check the terms of the chronic illness rider contract to see if the reinstatement provision of the rider is tied to the more stringent reinstatement provision of the life insurance policy. If so, the provision will allow for the reinstatement of a terminated policy and the attached chronic illness rider, but only with new evidence of insurability.

The potential danger of a reinstatement provision requiring evidence of insurability is that if the policy unintentionally lapses due to the insured having functional incapacity or a cognitive reason, it may also result in the insured being unable to pass the underwriting requirements needed to show evidence of insurability. Therefore, in such a case, the policy and chronic illness rider would remain lapsed.

Extension of benefits

All LTC policies and LTC riders are required to have this feature.

- The *extension of benefit* provision is a protection that allows for LTC benefits to still be paid on a lapsed policy if the insured can prove he or she would have qualified for benefits prior to the date their policy was terminated. When a LTC rider is added to a life insurance policy, this provision allows the policy owner to go back and capture LTC benefits the insured would have qualified for on their policy if they had applied for their rider benefits while the policy was still in force (if allowed by the state of issue). The policy is still considered lapsed for purposes of the death benefit; therefore, the only benefits that will be paid are the LTC benefits the insured would have qualified for prior to the termination of the policy.

Chronic Illness riders are not required to offer this feature. Thus, even if the insured would have qualified for chronic illness benefits prior to policy lapse, there would be no contractual right to recapture benefits.

How benefits are paid

While many advisors are aware of the different benefit payment methods of rider benefits on life insurance, a brief refresher is shown, including the difference between indemnity and cash indemnity.

- *Reimbursement policies* – require bills and receipts to be submitted to the insurance company each month. The plan will only cover specific qualified LTC expenses, and the policy owner will only be reimbursed for the exact amount of qualifying expenses up to the maximum benefit amount. There are never any benefit dollars received in excess of actual qualifying expenses, even if expenses are less than the policy's maximum monthly benefit amount. Any remaining unused LTC benefits are paid as a death benefit. Some insurance companies allow for direct billing and reimbursement with the care service or facility, but keep in mind that many care services and facilities are not willing to participate in 3rd party billing and only want to bill the responsible party.
- *Indemnity policies* – will pay the entire maximum monthly LTC benefit amount. Maximum benefits that can be received will be tied in some manner to the Health Insurance Portability and Accountability Act (HIPAA) per diem in the year of claim. Most policies of this type require a certain level of licensed care services be used. The insurance company places no restrictions on how LTC benefits are used, and any benefits received that are not needed to pay for care services can be set aside for later use. Any unused LTC benefits are paid as a death benefit. Bills and receipts are generally not required once the claim is approved, but keep in mind that a few companies may ask for monthly proof of at least one billed service.
- *Cash indemnity policies* – will pay the entire maximum monthly LTC benefit amount. Maximum benefits that can be received will be tied in some manner to the HIPAA per diem in the year of claim. The insurance company places no restrictions on how LTC benefits are used; thus, benefits can be used to pay family members or less expensive informal caregivers to provide care. LTC benefits received that are not needed for the individualized needs of the insured can be set aside for LTC expenses that may occur after their LTC benefits have been paid in full. Any unused LTC benefits are paid as a death benefit. Once the claim is approved there is not monthly paperwork required to receive benefits.
- *Acceleration* – is the method used by chronic illness riders, and has the look and feel of indemnity. The entire qualifying benefit amount is received based on the type formula the policy uses to calculate benefits (dollar for dollar method, discount method, or lien with interest method). Some policies will tie the maximum amount that can be received in some manner to the HIPAA per diem in the year of claim. Any remaining unused LTC benefits are paid as a death benefit.

Differences at a glance

The purpose of the chart below is to provide an advisor a quick glance of features and benefits offered by each type LTC or chronic illness rider. This chart does not include all features or benefits an insurance company may offer, but

does provide a starting point to help an advisor sift through policy rider details he or she may be considering as solutions for a specific client's financial strategy.

	Dollar for Dollar LTC Rider	Dollar for Dollar Chronic illness Rider	Lien with Interest Chronic Illness Rider	Discounted Chronic Illness Rider
Internal Revenue Code Section	7702B ³	101(g)	101(g)	101(g)
Pays Permanent Claims	YES	YES	YES	YES
Pays Temporary Claims	YES	Most still NO but varies by company, check policy details ⁴	Most still NO but varies by company, check policy details ⁴	Most still NO but varies by company, check policy details ⁴
Method of benefit payment	Cash indemnity, indemnity or reimbursement	Acceleration	Acceleration	Acceleration
Actual LTC or Chronic Illness claim benefit is known at policy issue	YES	YES	YES	NO
Total pay-out from policy known at issue (Rider benefits plus remaining DB)	YES	YES	NO	NO
100% total policy death benefit paid if the rider is invoked prior to age 100	YES	YES	NO	NO
Minimum Guaranteed DB Available	YES, on most ⁵	NO	NO	NO
Unintentional Lapse Protection	YES	Not required	Not required	Not required
Reinstatement within 5 months of termination	YES	Not required	Not required	Not required
Extension of Benefits	YES	Not required	Not required	Not required
Life Insurance and other required licenses ⁶	YES	YES	YES	YES
State specific LTC CE requirements needed	YES ⁷	None	None	None

Checklist to cover with clients

When showing a LTC Rider or chronic illness rider to a client purchasing life insurance, the following check list should be covered and discussed. The conscientious advisor will want to be aware of the differentiating features when ascertaining whether a LTC Rider or chronic illness rider will meet client needs and expectations. Factors to consider include:

- Will temporary claims as well as permanent claims be covered, or only permanent claims?
- Is the rider underwritten and charged for, or included with the policy?
- If included with the policy, how are rider benefits calculated, and what is the resulting back end charge?
- Is the benefit amount known at policy issue and guaranteed — or — is the rider benefit calculated at time of claim and discounted (with a forfeiture of a portion of the death benefit)?
- How are rider benefits paid to the policy owner — cash indemnity, indemnity or reimbursement?
- Is monthly paperwork required in order to receive benefits?
- Are full rider benefits available when using informal caregivers?
- How much in total will the policy pay between the rider acceleration and final death benefit?

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- the amount of the issued policy (assuming no withdrawals or loans)?
 - or, an amount that is less than the issued policy and unknown until claim time and/or death?
 - Are there consumer policy protections to help avoid unintentional lapse of the policy?
 - Does the reinstatement provision of the rider require evidence of insurability?
 - Are there provisions contained that still may allow for benefits to be received even if a policy has unintentionally lapsed (extension of benefits qualification)?

Summary

In the end, the client's best interest should always be of first consideration when helping a client choose a solution for potential long-term care or chronic illness needs. Making sure your client understands the LTC or chronic illness coverage they are purchasing, as well as the consumer protections they may or may not receive with their coverage of choice will potentially lead to a better experience for all if and/or when a claim eventually arises.



¹ The American Association of Long Term Care Insurance, Sourcebook 2015-2016

² American Alzheimer's Association 2016 report

³ Most LTC riders are filed in this manner, however there are a few companies that file LTC riders under IRS Code §101(g) paired with NAIC LTC Model Regulations. These products may be referred to a long-term care and have the same consumer protection requirements as do LTC Riders filed under IRS Code § 7702B

⁴ Please refer to the insurance company's rider contract in the section referring to the payment of claims for specific details

⁵ Please refer to the insurance company's rider contract for details on the availability and amount of any minimum death benefit guarantee offered.

⁶ Some states require a health insurance license. In addition, there may be other underlying licenses needed to sell the base life insurance policy.

⁷ Most states (but not all) have a minimum LTC CE requirement that must be maintained to be able to sell LTC Riders or any LTC product.

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