

FINANCIAL SERVICES

POSSIBILITIES

*Long-Term Care Partnership Policies***OVERVIEW**

To encourage more individuals to purchase long-term care insurance, many states have enacted Partnership programs that authorize private insurers to sell state-approved long-term care Partnership policies. This article provides an overview of Partnership policies.

What are Long-Term Care Partnership Policies?

The high cost of long-term care has placed a financial burden on individuals and state Medicaid programs. As the number of older Americans grows, the strain is likely to worsen, and containing Medicaid costs has become a priority for states and the federal government. To encourage more individuals to purchase long-term care insurance, many states have enacted Partnership programs that authorize private insurers to sell state-approved long-term care Partnership policies.

Partnership policies are designed to help individuals plan for their long-term care needs, while minimizing the risk of impoverishment should the policyholder need long-term care. They are similar in many respects to traditional long-term care insurance policies, but must include inflation protection, asset protection and other features in order to qualify as Partnership policies. Individuals who purchase Partnership policies, then expend policy benefits on long-term care services, will qualify for Medicaid without having to first spend all or most of their remaining assets (assuming they meet income and other eligibility requirements). This gives people the incentive to buy long-term care insurance, potentially limiting state Medicaid spending.

Some Background

In 1992, four states (California, Connecticut, Indiana and New York) launched long-term care Partnership programs. Other states intended to develop programs, but the Omnibus Budget Reconciliation Act of 1993 (OBRA) halted the

implementation of new programs due to the requirement that states recover assets from anyone receiving Medicaid. However, the four states with demonstration projects were allowed to continue selling Partnership policies under the pilot program.

The moratorium on new Partnership programs ended in 2006, after the Deficit Reduction Act of 2005 (DRA) authorized all states to adopt long-term care Partnership programs. As a result, many states have authorized the sale of Partnership policies, and others are still in the process of implementing them.

Partnership Policies: A solution to Rising Medicaid Costs?

Medicaid is the single largest payer of nursing home bills in America. Although it's intended to be the last resort for people who have no other way to pay for long-term care services, more and more Americans with moderate incomes are relying on Medicaid, due to the rapidly rising cost of long-term care.

But as a program for individuals with limited income and assets, Medicaid has strict eligibility requirements. To qualify in most states, residents must meet certain medical criteria, and both their income and the value of their assets must fall below certain levels. Residents who have income and assets that are higher than state mandated levels may have to "spend down" or, in some cases, legally transfer income and assets in order to become eligible for Medicaid. States have the right to seek reimbursement from recipients for Medicaid payments made on their behalf, and can seek reimbursement from their estates, although they don't always do so.

Partnership policies include incentives to encourage individuals to purchase long-term

Partnerships policies—continued on page 2

inside

4 *Bridging the Gap:
Resolving Projected
Retirement Income
Shortfalls*

7 *Funding Long-Term
Care Insurance:
Changes Create
New Opportunities*





Medicaid asset protection is the main feature that distinguishes a Partnership policy from a traditional long-term care policy. This type of protection is valuable to individuals who would otherwise become impoverished and left with little or nothing to pass along to their heirs in the event they need to rely on Medicaid.

care insurance, instead of relying on Medicaid. Although any resident of a state in which Partnership policies are offered can purchase such a policy, state Partnership programs primarily target individuals with moderate income and assets. These are individuals who can afford reasonable long-term care insurance premiums, but who can't afford to pay for long-term care out-of-pocket for more than a short period of time, and thus may eventually need to rely on Medicaid after their assets are exhausted. (Wealthier individuals often don't need to rely on Medicaid in the first place, and individuals with very limited means will likely qualify for Medicaid right away, and may have few assets to protect.)

Although the financial impact may not be known for years, the hope is that when offered a long-term care insurance product with built-in Medicaid asset protection and other features, such as inflation protection, Americans with moderate incomes will increasingly plan for long-term care, thus delaying or even eliminating the need to rely on Medicaid.

What Makes Partnership Policies Different?

In many respects, Partnership policies authorized by the DRA are very similar to traditional long-term care policies, and have many of the same features and benefits. Qualifying for a Partnership policy will be the same as qualifying for a traditional long-term care policy—

applicants will still need to meet underwriting requirements of the issuing insurance company. However, Partnership policies must meet several special requirements. Although Partnership policies may vary somewhat from state to state, they all must meet specific DRA guidelines. According to these guidelines, all new Partnership policies must:

- Offer Medicaid asset protection using the dollar-for-dollar asset protection model,
- Include automatic inflation protection if issued to anyone under age 76,
- Follow the consumer protection guidelines of the National Association of Insurance Commissioners (NAIC) Long-Term Care Insurance Model Act, and,
- Be tax qualified.

The Dollar-for-Dollar Asset Protection Model

Medicaid asset protection is the main feature that distinguishes a Partnership policy from a traditional long-term care policy. This type of protection is valuable to individuals who would otherwise become impoverished and left with little or nothing to pass along to their heirs in the event they need to rely on Medicaid.

All Partnership policies include some type of asset protection, but DRA-authorized Partnership policies must use a specific model called the dollar-for-dollar asset protection model. Under this model, the amount of assets that are protected from Medicaid spend-down requirements equals the dollar value of benefits paid by the long-term care insurance contract. This is in addition to any asset protection limit that already applies.

Example: Maria purchases a Partnership policy with a maximum benefit of \$150,000. She enters a nursing home, exhausts her benefits, and applies for Medicaid. According to eligibility guidelines in her state, normally she would be entitled to keep only \$2,000 in assets, but because she has purchased a Partnership policy, Maria will be able to keep \$152,000 in assets, and still qualify for Medicaid (assuming, of course, that she meets other eligibility requirements).



Additionally, assets protected by a Partnership policy are not subject to estate recovery. They can be given away without affecting the insured's Medicaid eligibility, and when the insured policyholder dies, the state will not attempt to recover those assets from the policyholder's estate.

Caution: It's important not to confuse asset protection with income protection. Even though insured individuals can retain some of their assets, they may still need to spend their income on long-term care before Medicaid covers their expenses.

Plans in the four original Partnership states are exempt from the new guidelines and use varying asset protection models. California and Connecticut use the dollar-for-dollar asset protection model, while New York uses both the dollar-for-dollar model and a different asset protection model called the total assets model. The total assets model requires individuals to purchase a specific number of years of long-term care coverage (three to six years). In exchange, the individual receives total asset protection. Indiana uses a hybrid model—policies with benefit amounts up to a certain level offer dollar-for-dollar asset protection, while policies with benefits exceeding that amount offer total asset protection.

Inflation Protection Provisions

Inflation protection is another key feature of long-term care Partnership policies. Inflation protection means that benefits will increase over time. Although it may substantially increase premium cost, it helps the coverage keep pace with rising long-term care costs, especially since many years may pass between the time the policy is purchased and when benefits are needed. Traditional policies might offer inflation protection, but all Partnership policies are required to include some form of inflation protection, according to the following guidelines.

For individuals who are:

- Under age 61 at the date of purchase: The policy must include annual compound inflation protection.

- Ages 61-76 at the date of purchase: The policy must include some type of inflation protection (but not necessarily annual compound inflation protection).
- Age 76 or older at the date of purchase: The policy is not required to include inflation protection, but may offer it.

Compound inflation protection increases the daily benefit each year, essentially increasing the amount of asset protection each year. Although Partnership policies in the original four states use a 5 percent inflation factor, new Partnership states have the discretion to use any inflation factor they choose.

For individuals age 61 or older, the type of inflation protection that may be offered will vary. One available option may be future purchase inflation protection. With this type of inflation protection, policyholders will periodically be given the chance to purchase an increased daily benefit with no health underwriting.

Tax-Qualified Policies

Long-term care policies offered under state Partnership programs must be tax qualified. Policies are considered tax qualified if they meet standards specified by the Health Insurance Portability and Accountability Act (HIPAA). Part or all of the premiums paid for a tax-qualified policy may be deductible as a medical expense from federal income taxes. Premiums may be deductible for policyholders who itemize and whose total qualified medical expenses exceed 7.5 percent of their annual adjusted gross income, up to certain age-related limits. In addition, benefits received will generally not be considered taxable income. State income tax deductions or credits may also be available.

Questions and Answers

If someone purchases a Partnership policy, will he or she automatically qualify for Medicaid?

No. Medicaid eligibility is never automatic. To qualify, an individual must meet state eligibility requirements. It's possible that even if someone exhausts his or her Partnership policy benefits, he or she will not qualify for Medicaid.



Additionally, assets protected by a Partnership policy are not subject to estate recovery. They can be given away without affecting the insured's Medicaid eligibility, and when the insured policyholder dies, the state will not attempt to recover those assets from the policyholder's estate.

■ Bridging the Gap

Resolving Projected Retirement Income Shortfalls

OVERVIEW

If you find yourself with a shortfall in projected retirement income—don't panic. This article discusses several methods of coping with projected income shortfalls.



The longer you delay retirement, the longer you can contribute to your IRA or employer-sponsored retirement plan. However, if you have a traditional IRA, you must start taking required minimum distributions (and stop contributing) when you reach age 70½.

What is a Projected Income Shortfall?

When you determine your retirement income needs, you make your projections based on the type of lifestyle you plan to have and the desired timing of your retirement. However, you may find that reality is not in sync with your projections, and it looks like your retirement income will be insufficient for the rate you plan to spend it. This is called a projected income shortfall. If you find yourself in such a situation, finding the best solution will depend on several factors, including the following:

- The severity of your projected shortfall.
- The length of time remaining before retirement.
- How long you need your retirement income to last.

Several methods of coping with projected income shortfalls are described in the following sections.

Delay Retirement

One way of dealing with a projected income shortfall is to stay in the workforce longer than you had planned. This will allow you to continue supporting yourself with a salary rather than dipping into your retirement savings.

What it Means

Delaying your retirement could mean that you continue to work longer than you had originally planned. Or, it might mean finding a new full- or part-time job and living off the income from this job. By doing so, you can delay taking Social Security benefits or distributions from retirement accounts. The longer you delay tapping into these sources, the longer the money will last when you do begin taking it. While you might hesitate to start on a new career path late in life, there may actually be certain unique opportunities that would not have been available earlier in life. For example, you might consider entering the consulting field, based on the expertise you have gained through a lifetime of employment. This decision may involve tax issues, so it may be beneficial to review its tax impact with a tax professional.

Effect on Social Security Benefits

The Social Security Administration has set a “normal retirement age,” which varies between

65 and 67, depending on your date of birth. You can elect to receive Social Security retirement benefits as early as age 62, but if you begin receiving benefits before your normal retirement age, your benefits will be decreased. Conversely, if you elect to delay retirement, you can increase your annual Social Security benefits. There are two reasons for this. First, each additional year that you work adds an additional year of earnings to your Social Security record, resulting in potentially higher retirement benefits. Second, the Social Security Administration gives you a credit for each month you delay retirement, up to age 70.

Effect on IRA and Employer-Sponsored Retirement Plan Distributions

The longer you delay retirement, the longer you can contribute to your IRA or employer-sponsored retirement plan. However, if you have a traditional IRA, you must start taking required minimum distributions (and stop contributing) when you reach age 70½. If you fail to take the minimum distribution, you will be subject to a 50 percent penalty on the amount that should have been distributed. If you have a Roth IRA, you are not required to take any distributions while you are alive, and you can continue to make contributions after age 70½ if you are still working. Minimum distribution rules do not apply to money in qualified retirement plans until you reach age 70½ or retire (whichever occurs later), unless you own 5 percent or more of your employer.

Other Considerations

Under the federal Age Discrimination in Employment Act, individuals 40 years of age or older are protected against employment discrimination based on age. However, employers may have legitimate concerns about hiring an individual of retirement age. Prospective employers may believe older employees will have greater health care needs, require more sick leave, and tend to be short-term employees. You should be aware of these concerns and have a strategy for dealing with them if you plan to seek new employment after you have reached retirement age.

Save More Money

You may be able to deal with projected retirement income shortfalls by adjusting your spending habits, thus allowing you to save more money for retirement. Depending on how many years you have before retirement, you may be able to get by with only minor changes to your spending habits. However, if retirement is fast approaching, drastic changes may be needed. Saving even a little money can really add up if you do it consistently and earn a reasonable rate of return. Make permanent changes to your spending habits and you'll find your savings lasting even longer.

Make Major Changes to Your Spending Patterns

If you expect to fall far short of your retirement income needs, or if retirement is only a few years away, you may need to change your spending patterns drastically to save enough to cover the shortfall. You should create a written budget, so you can easily see where your money goes and where you can reduce your spending. The following are some suggested changes you may choose to implement:

- Consolidate your loans to reduce your interest rate and/or monthly payment. Consider using home equity financing for this purpose.
- Refinance your home mortgage if interest rates have dropped since you took the loan.
- Reduce your housing expenses by moving to a less expensive home or apartment.
- Sell your second car, especially if it is only used occasionally.

Make Minor Changes to Your Spending Patterns

Minor changes can also make a difference. You'd be surprised how quickly your savings add up when you implement several small changes to your spending patterns. If your expected shortfall is minor, or if you have many years before you plan to retire, making such small changes to your spending habits may be enough to correct this problem. The following are several areas you might consider when adjusting your spending patterns:

- Buy only the insurance you really need. For example, consider canceling collision insurance on an older vehicle.
- Shop for the best interest rate whenever you need a loan.

- Switch to a lower interest credit card. Transfer your balances from higher interest cards and then cancel the old accounts.
- Eat dinner at home, and carry "brown-bag" lunches instead of eating out.
- Consider buying a well-maintained used car instead of a new car.
- Subscribe to the magazines and newspapers you read instead of paying full price at the newsstand.
- Cut down on utility costs and other household expenses.
- Get books and movies from your local library instead of buying or renting them.
- Plan your expenditures and avoid impulse buying.

Hold on to the Money You Save

Keep in mind that the money you save should be earmarked for your retirement. It should not be frittered away on minor expenditures and impulse purchases. The point of reducing your spending is to overcome projected income shortfalls, not to indulge yourself at end-of-season clearance sales. The money you save should be put away immediately. If you can take advantage of an IRA or other similar retirement plan, consider doing so. Any growth such a plan may experience will occur on a tax-deferred basis.

Continue Saving During Your Retirement

Don't think of your retirement date as your deadline for saving. Instead, continue to save money throughout your retirement years. Saving may become more difficult after retirement as a result of reduced income and potentially increased medical expenses. But you can work part-time during retirement and take other steps to keep saving. Putting away just a little each month can make a significant difference in how long your money will last.

Caution: Note that some of the powerful tax-deferred savings vehicles you took advantage of while working may no longer be available to you during retirement. To participate in a 401(k), for example, you must be employed by a company that offers such a plan and must meet the employer's eligibility requirements (e.g., length of service). IRAs only allow you to contribute



If you expect to fall far short of your retirement income needs, or if retirement is only a few years away, you may need to change your spending patterns drastically to save enough to cover the shortfall. You should create a written budget so you can easily see where your money goes and where you can reduce your spending.

earned income (i.e., job earnings) and generally don't permit any contributions after age 70½ (except in the case of Roth IRAs). So, while you can certainly continue saving during retirement, your options may be more limited.

Consider Greater Investment Risk

If you are facing a projected income shortfall, you may want to revisit your investment choices, particularly if you're still at least 10-15 years from retirement. If you're willing to accept more risk, you may be able to increase your potential return. However, there are no guarantees; as you take on more risk, your potential for loss grows, as well. Be sure to consult your financial professional before you make any changes to your portfolio.

Make Sure Your Level of Risk is Appropriate for Your Long-Term Objectives

It's not uncommon for individuals to make the mistake of investing too conservatively for their retirement goals. For example, if a large portion of your retirement dollars is in low interest earning fixed-income investments, be aware that the return on such investments may not outpace the rate of inflation. By contrast, equity investments (i.e., stocks and stock mutual funds) generally expose you to greater investment risk, but have the potential to provide greater returns.

Re-evaluate Your Standard of Living in Retirement

If your projected income shortfall is severe enough, or if time is too tight, you may realize that no matter what measures you take, you will not be able to afford the lifestyle you want during your retirement years. You may simply have to accept the fact that your retirement will not be the jet-setting, luxurious, permanent vacation you had envisioned. In other words, you will have to lower your expectations and accept a more realistic standard of living. Recognize the difference between the things you want and the things you need and you'll have an easier time deciding where you can make adjustments. Here are a few suggestions:

Reduce Your Housing Expectations

Perhaps you've always planned to live in a luxury condominium community in Palm Beach

when you retire. Realize that this goal may not be realistic. If you are facing a severe income shortfall, you might have to shop around for a more affordable housing option in a less exclusive location.

Cut Down on Travel Plans

Maybe you'd always planned an extended tour of Europe or a cruise around the world to celebrate your retirement. You may have to downgrade these plans to a driving trip to visit relatives or a train trip across the Rockies. Simple trips can be just as much fun as extravagant vacations, and they don't put as big a dent in your retirement funds.

Consider a Less Expensive Automobile

You may dream of driving a shiny new Cadillac off the dealer's lot right after you collect your retirement gift from your employer, but shiny new Cadillacs come with big, thick payment books. Consider purchasing a used car of the type you want. If you must have a new car, think about buying a less expensive model.

Lower Household Expenses

There are numerous ways to decrease your everyday expenses. You might find that simply cutting back on your spending will help stretch your retirement dollar. For instance, you could eat out less often, use public transportation instead of your car, or set your home thermostats slightly lower in the winter. ■

CONTACT

- Talk to your local Eide Bailly financial advisor
- Call 866.740.4100 for more information



There are numerous ways to decrease your everyday expenses. You might find that simply cutting back on your spending will help stretch your retirement dollar. For instance, you could eat out less often, use public transportation instead of your car, or set your home thermostats slightly lower in the winter.

■ Funding Long-Term Care Insurance

Changes Create New Opportunities

The Pension Protection Act of 2006 offers an exciting feature for the funding of long-term care insurance protection through the use of life insurance and annuity contracts. Effective January 2010, the Act provides new tax rules for long-term care insurance that's provided by a rider on, or as part of, an annuity contract, and also modifies the former tax rules for long-term care insurance coverage provided in conjunction with a life insurance contract.

The rules for tax-free exchanges of certain insurance contracts are expanded. No gain or loss is recognized on the exchange of a life insurance contract, an endowment contract, an annuity contract, or a qualified long-term care insurance contract for a qualified long-term care insurance contract.

One group that may see benefits of this rule change are owners of non-qualified annuities, (those funded with after-tax dollars), holding significant investment gains within the annuity. They are now able to exchange the annuity to pay for qualified long-term care insurance contracts, and the owner may be able to avoid taxes on the gain portion of the annuity. The value of this benefit would vary based on the tax situation of the annuity owner, and the amount of gain within the annuity. The higher the owner's tax rate and the greater their annuity investment gain, the larger their tax savings. One point to

note is that the ownership of the annuity must match the ownership of the long-term care policy.

Another group that may benefit from the changes are owners of linked benefit annuity and life insurance products. These products combine the annuity or life insurance contract with a long-term care benefit. Prior to the rule change, the payments for the long-term care benefit were taxed as distributions to the extent of gain in an annuity contract and in a modified endowment life insurance contract.

No deduction as a medical expense is allowed for any payment made for coverage under a qualified long-term care insurance contract if the payment is made as a charge against the cash value of an annuity contract or the cash surrender value of a life insurance contract.

The rules for these exchanges and benefits are complicated. We encourage you to contact an Eide Bailly financial services representative and tax advisor to guide you through the various options. ■

CONTACT

- Talk to your local Eide Bailly financial advisor
- Call 866.740.4100 for more information

OVERVIEW

This article highlights opportunities for funding long-term care insurance protection through the use of life insurance and annuity contracts, provided by the Pension Protection Act.



POSSIBILITIES is distributed with the understanding that the information contained does not constitute legal, accounting or other professional advice. It is not intended to be responsive to any individual situation or concerns as the contents of the publication are intended for general informational purposes only. Content provided by Forefield, Inc. Neither Forefield Inc. nor Forefield Advisor™ provides legal, taxation or investment advice. All the content provided by Forefield is protected by copyright. Forefield claims no liability for any modification to its content and/or information provided by other sources. Copyright 2010 Forefield Inc. All Rights Reserved.

Questions and information for publication can be submitted to your Eide Bailly representative or to the editors of the newsletter.

To view this and previous issues of **POSSIBILITIES**, visit www.eidebailly.com/publications

Managing Editor: Liz Stabenow
Assistant Editor: Lisa Dahlen and Theresa Hall

An Independent Member Firm of HLB International

Financial Advisor is a Registered Representative of and offers securities through Securities America, Inc. Member FINRA and SIPC. Investment Advisory Services offered through Eide Bailly Advisors, LLC, a Registered Investment Advisor. Eide Bailly Financial Services, LLC is the holding company for Eide Bailly Advisors, LLC. Eide Bailly Financial Services and its subsidiaries are not affiliated with Securities America companies.



4310 17th Ave S
PO Box 2545
 Fargo ND 58108-2545

RETURN SERVICE REQUESTED

Partnership policies—from page 3

Do any residency restrictions apply to the sale of Partnership policies?

An individual purchasing a long-term care policy must be a resident of the state in which the policy is purchased.

What happens if someone purchases a Partnership policy in one state, then moves to another?

With Partnership policies, portability is a major concern. Although Partnership policy insurance protection is portable, asset protection is not. This means that if someone insured under one state's Partnership program moves to another state, he or she can receive Partnership policy benefits, but his or her assets will not be shielded from Medicaid recovery in the new state. Fortunately, most states that offer Partnership policies have decided to participate in a national reciprocity agreement that allows state residents to retain dollar-for-dollar asset protection in any other state that participates in the agreement, assuming they qualify for Medicaid in their new state of residence. States can opt out of

participating, however, so individuals thinking about purchasing a long-term care Partnership policy should consider the laws of the state in which they currently reside, and, if possible, the laws of any state in which they plan to reside someday.

Will states with new Partnership programs automatically convert existing traditional long-term care policies into Partnership policies?

No. Federal law prohibits the grandfathering of traditional long-term care policies. However, some states may allow insurers to exchange existing traditional policies for Partnership policies. ■

CONTACT

- Talk to your local Eide Bailly financial advisor
- Call 866.740.4100 for more information