

Safeguarding Your Future: Preparing for Possible Long-Term Care Costs in Retirement

Planning for retirement isn't just about building a nest egg—it's about safeguarding your future by addressing potential risks that could undermine financial security. One of the most significant yet often overlooked risks is the possibility of long-term care needs. With increasing life expectancies, 7 out of 10 Americans, age 65 or older, will require some form of long-term care due to illness, injury, or age-related conditions.¹ According to a Congressional Research Service report updated in September 2023, total spending on Long-Term Services and Support (LTSS) from all sources in 2021 was \$467.4 billion. Medicaid topped the list at \$207 billion (44.3%) but seniors must meet strict income and asset guidelines to qualify. The report indicated that out-of-pocket expenditures totaled \$63.6 billion, or 13.6% of total LTSS spending.² This data underscores the importance of incorporating potential long-term care expenses when planning for retirement.

The costs associated with long-term care—whether it's nursing home stays, in-home care, or assisted living facilities—can be financially devastating if not adequately planned for. Failing to consider these expenses can rapidly deplete retirement savings, leaving you, your spouse, or extended family members financially vulnerable. Implementing strategies within your retirement plan to address potential long-term care costs is crucial to maintaining financial independence, protecting your assets, and preserving your quality of life throughout retirement. By proactively incorporating long-term care considerations, you can mitigate the financial risks and feel confident that you and your loved ones are prepared for the future. Remember, early preparation is vital to reducing the impact of these potential costs on your retirement savings.



Understanding Long-Term Care

Long-term care primarily involves custodial care, which can also include medical care, depending on your needs. Custodial care is centered on assisting individuals with activities of daily living (ADLs), such as bathing, dressing, eating, and toileting. This type of care is non-medical and is typically provided by caregivers or aides who may not have specialized medical training but play a crucial role in supporting those in need.

However, long-term care can also include elements of medical care. For example, individuals with chronic conditions or those recovering from serious health events may require skilled nursing care or rehabilitative therapy such as physical, occupational, or speech therapy. Licensed healthcare professionals administer these services.

Understanding the difference between custodial and medical (skilled) care is crucial. Custodial care is non-medical assistance with daily tasks or ADLs, often provided in home settings, assisted living facilities, or nursing homes. On the other hand, medical care involves treatment and services from trained medical professionals, such as administering medications, wound care, physical therapy, and monitoring health conditions.

Medicare and Long-Term Care

A common and often costly misconception is that Medicare, the federal health insurance program primarily designed to cover Americans age 65 and older, with some exceptions for younger individuals with disabilities, covers the cost of long-term support and services. Medicare, including Medicare Supplement Insurance (Medigap), generally does not cover most long-term care services, particularly custodial care.³ However, Medicare may cover short-term skilled nursing care and rehabilitative services under specific circumstances.

What Medicare covers:

- **Skilled Nursing Facility Care:** Medicare Part A covers up to 100 days of care in a skilled nursing facility per benefit period. However, this coverage is only available after a qualifying hospital stay of at least three days. The care provided by the skilled nursing facility must be medically necessary and include services such as physical therapy or post-acute recovery care.⁴
- **Home Health Care:** Medicare covers limited home health services if the patient is homebound and needs intermittent skilled care, such as nursing services or physical therapy.⁵
- **Hospice Care:** Medicare covers hospice services for terminally ill patients with a prognosis of six months or less, focusing on palliative care rather than curative treatment.⁶

While Medicare may cover short-term skilled nursing care after a hospital stay, it does not extend to ongoing custodial care needs in a nursing home or assisted living facility. This distinction is vital for those planning for long-term care expenses in retirement.



Median Cost of Care

A significant factor in how much you might spend on this care will depend upon the setting in which your care occurs. For example, long-term care often involves paying for service providers in various settings, including home health aides, community-based facilities such as adult day care, assisted living facilities, and nursing homes. These services can be costly, depending on factors such as care needs, age, and health conditions. According to the recent data collected by Genworth, the annual median cost of long-term care in 2023 was:⁷

Private Room in a Nursing Home	\$116,900
Semi-Private Room in a Nursing Home	\$104,028
Private Room in an Assisted Living Facility	\$64,200
Home Health Aide	\$75,504

Preparing well before needing care can help avoid financial stress and the emotional strain of getting the necessary care.

Reducing Your Risk of Needing Long-Term Care

The need for long-term care can be challenging to predict and may arise suddenly or gradually due to aging or chronic health conditions. Adopting healthy habits such as good nutrition, regular exercise, avoiding smoking and alcohol consumption, staying socially active, and receiving regular healthcare check-ups can reduce the risk of developing long-term illnesses. Consulting with a healthcare provider about your medical history, family background, and lifestyle can help identify personalized actions to improve your health and delay the potential need for extensive care.



Climbing Costs

For years, the cost of LTC has steadily increased, along with the costs of goods and services faced by seniors, such as food, gas, and housing. For instance, according to the latest Genworth Cost of Care Survey, the median cost of home health aide services increased by 10% between 2022 and 2023. This increase was higher than the growth in the median cost for a private room in a nursing home, which increased by 4.92% annually over the same period. Interestingly, the increase in assisted living facility costs was a modest 1.36% from 2022-2023, but between 2021-2023, it was a staggering 18.89%.⁸ The Genworth Study attributed the increase in long-term care costs to both inflation and a shortage of workers.

As long-term care costs continue to rise, individuals and families must plan ahead. Even though Medicare does not cover the high cost of long-term care in a nursing home or other facility, other options are available to help with these expenses. This could include utilizing government assistance programs such as Medicaid or Veterans benefits, if applicable, saving money specifically for long-term care, purchasing LTC insurance, or exploring other strategies to cover these potential costs.

Government assistance programs

Each state manages Medicaid, a federal program that provides coverage for medical expenses and long-term care costs for individuals with low income and limited assets. However, to qualify for Medicaid, you must meet strict financial criteria, often requiring spending down your assets to become eligible. While Medicaid serves as a vital safety net if you have limited resources, it may not be the best fit if you want more control over your care options, to leave a financial legacy for loved ones, or to support charitable causes. For more information about Medicaid in your state, visit <https://www.medicaid.gov/about-us/where-can-people-get-help-medicaid-chip/index.html#statemenu>.

If you have higher assets and income, you may explore specific strategies designed to protect assets to qualify for Medicaid, particularly for nursing home care. These strategies can be complex and may not always succeed in reducing exposure to high out-of-pocket costs. Therefore, you should consult qualified financial and tax professionals along with an elder law attorney to navigate these options to determine if these strategies may work for your situation.

Another potential source of LTC assistance is the Veterans Health Administration, which benefits qualifying veterans and their eligible dependents. If you are a Veteran, you may qualify for coverage for assisted living, in-home care, or residential care.⁹ Additionally, certain states provide programs to help residents manage long-term care expenses, so it is crucial to explore all available options when planning for future care needs.

Self-Insurance

Using personal savings to cover the cost of long-term care is a common approach, especially if you do not qualify for Medicaid or prefer not to rely on government programs. Setting aside funds for long-term care expenses can provide greater flexibility and choice in selecting care options, such as in-home care, assisted living, or nursing home facilities. Personal savings can come from various sources, including retirement accounts, investment portfolios, or liquid assets. This strategy lets you control your care decisions and maintain a desired quality of life. However, if you decide to use retirement accounts such as 401(k)s or IRAs to cover LTC expenses, you should know the potential tax ramifications of withdrawals. Consult with a financial or tax professional to understand the implications.

Also, long-term care costs can be substantial. Factoring in the potential for increased care needs over time due to extended life expectancies or progressive health conditions could dwindle savings quickly. Relying exclusively on retirement savings could reduce available funds for other retirement goals. If you plan to self-fund all or part of your long-term care, it's essential to start building a diversified savings plan early. This can include setting aside specific investment accounts for long-term care costs and taking full advantage of tax-advantaged vehicles like a Health Savings Account (HSA). HSAs allow you to save for qualified medical expenses, including certain long-term care services, with the benefit of tax-free contributions, growth, and withdrawals when used for medical purposes.¹⁰ By creating a well-rounded savings strategy, you can ensure you have the financial flexibility to cover care costs without compromising your broader retirement goals.



Unpaid Family Caregivers

According to an AARP study, *Valuing the Invaluable*, approximately 38 million unpaid caregivers, or 11.5% of the total population, cared for loved ones in 2023. The value of that care is nearly \$600 billion, equating to 36 billion hours dedicated to caring for loved ones.¹¹ Much of that responsibility has fallen to those often called the “sandwich generation” or those who care for their children and aging parents. These individuals are effectively “sandwiched” between the needs of two generations, often feeling the weight of caregiving responsibilities on their shoulders while juggling their own personal and financial obligations.

Relying on familial caregivers can be equally emotionally stressful to the caregiver and the one needing care. Financially, caregivers may be ill-equipped to take on the additional costs of caring for loved ones. Without adequate savings, the parent requiring care may feel like a burden. To avoid such emotional and financial tolls, having alternative options for a potential long-term care need and speaking openly to family members is crucial.



Traditional Long-Term Care Insurance

The long-term care (LTC) insurance market has evolved considerably since its introduction in the 1960s. Standalone LTC policies are designed to cover services not typically included in health insurance or Medicare, such as in-home care, assisted living, or nursing home stays. These policies can be a viable option for those who can afford the premiums—now and in the future, even with likely rate increases. Premiums are based on factors like age, gender, health, and location and must be paid annually for the life of the policy. One downside is that these policies accumulate no cash value, meaning the premiums paid are forfeited if no long-term care event occurs, like home and auto insurance.

Though standalone LTC policies may not cover all long-term care costs, they can significantly reduce out-of-pocket expenses. However, it's important to weigh the risk of paying for coverage that might never be needed, as premiums can be high and increase over time. Letting the policy lapse could result in lost benefits with no premium refund, leaving individuals without coverage when they need it most.

For those concerned about “use it or lose it” scenarios, alternatives like hybrid policies, which combine life insurance or annuities with long-term care benefits, may offer a more flexible approach while still providing coverage.



Asset-Based Long-Term Care Options

Asset-based long-term care (LTC) solutions are more flexible than traditional standalone policies. These hybrid policies provide coverage for unexpected long-term care needs and offer the option to use the funds for other purposes, such as retirement income or a life insurance death benefit. This flexibility allows policyholders to manage risk while avoiding future premium increases that can occur with standalone LTC coverage. Essentially, hybrid policies combine multiple financial goals into one product, providing retirement income from an annuity or life insurance benefits with the option to pay for long-term care if necessary. Additionally, hybrid policies often have less stringent underwriting requirements than standalone LTC policies, making it easier for individuals to qualify for long-term care benefits.

Hybrid Life Insurance and LTC Policies

If long-term care becomes necessary, hybrid policyholders can access a portion of the death benefit to cover eligible long-term care expenses. When some lifetime benefits are used for care, the remaining death benefit paid to beneficiaries will likely be reduced accordingly.

Hybrid policies come in various formats, with two common types being linked-benefit policies and life insurance policies with long-term care (LTC) riders. Linked-benefit policies typically offer a fixed death benefit and a capped LTC benefit. The death benefit decreases as LTC benefits are used, but this accelerated payout provides much-needed financial support at a critical time.

Alternatively, a life insurance policy with an LTC rider is ideal for individuals primarily seeking life insurance coverage, with the added flexibility of accessing LTC benefits if needed. This structure allows policyholders to tap into a portion of the death benefit for care while keeping the focus on providing life insurance coverage. Importantly, in both models, the life insurance component is typically a permanent policy, such as whole or universal life, rather than term insurance, ensuring lifelong coverage.

Long-term Care Annuities

This product combines long-term care insurance with an annuity, offering a safety net for potential long-term care (LTC) expenses and a tax-advantaged investment that can provide retirement income. The annuity grows tax-deferred; while offering a source of funds to pay for long-term care, should the need arise. If certain conditions are met, gains used to pay for LTC expenses are tax-free. If long-term care isn't required, the annuity can still serve as a source of retirement income or be passed on to beneficiaries.

Hybrid annuity-LTC policies are an efficient way to plan for future care needs while preserving flexibility. They allow individuals to protect against the high costs of long-term care while maintaining the potential for a death benefit or supplemental retirement income. As with any insurance product, it's essential to carefully review the policy's terms and conditions and consider the insurance company's financial strength, ensuring long-term stability for both retirement and LTC needs.

Deductibility of LTC Premiums

Under the Health Insurance Portability and Accountability Act of 1996 (HIPAA), the federal government allows the deductibility of premiums paid for qualified long-term care (LTC) insurance contracts, subject to certain conditions.¹² If you itemize deductions on your tax return, LTC premiums are considered unreimbursed medical expenses and may be deductible to the extent that they exceed 7.5% of your adjusted gross income (AGI). The amount of the deduction is capped based on age, with the following limits for 2025¹³:

Age 40 and below:	\$480
Age 41-50	\$900
Age 51-60	\$1,800
Age 61-70	\$4,810
Age 71 and older	\$6,020

The deduction for long-term care (LTC) premiums applies to individuals who pay premiums for themselves, their spouse, or dependents. In the case of business owners, they may be eligible to deduct up to 100% of premiums paid for qualified LTC insurance contracts. To ensure you're maximizing these tax benefits, it's essential to consult a tax advisor. They can help you navigate the rules and optimize your deductions, making your LTC premium payments as tax-efficient as possible.

Qualified Long-Term Care Contracts and Tax-Free Benefits

The IRS treats qualified long-term care contracts as accident and health insurance contracts. The amounts you receive from them are excludible from income. You must file IRS Form 8853 with your tax return to claim the exclusion. To be considered a qualified long-term care contract eligible for favorable tax treatment, the insurance contract must only provide coverage for qualified long-term care services and must also meet the following criteria:¹⁴

1. Be guaranteed renewable;
2. Not provide for a cash surrender value or other money that can be paid, assigned, pledged, or borrowed;
3. Provide that refunds, other than refunds on the death of the insured, and dividends only be used to reduce future premiums or increase future benefits;
4. In most cases, not pay or reimburse expenses covered by Medicare.





Leveraging Asset-Based Solutions for Tax Benefits

Most traditional long-term care insurance policies offer both the deductibility of premiums and tax-free benefits for long-term care services, provided specific IRS conditions are met. However, the Pension Protection Act of 2006 expanded these tax advantages further, benefiting more consumers by allowing a tax-free 1035 exchange of an existing life insurance or non-qualified annuity contract into a qualified long-term care policy, effective since 2010. This provision allows policy owners to leverage the accumulated value in an existing annuity to fund a qualified LTC policy without triggering taxation on the gains and take advantage of potential deductions and tax-free benefits.¹⁵

In addition, some insurance companies offer hybrid policies that combine annuities or life insurance while meeting the requirements of a qualified long-term care contract. These hybrid products meet strict IRS criteria, allowing policyholders to access tax-free distributions for future long-term care needs. These options offer consumers a more flexible way to prepare for long-term care while maximizing tax efficiency.

It's important to consult with a knowledgeable financial professional and tax advisor to determine which insurance companies offer these tax-favored asset-based policies, whether these strategies suit your situation, and to maximize potential tax benefits.

Planning Considerations:

Retirees and near-retirees evaluating the different options for paying long-term care expenses should consider the following factors:

- **Cost:** Review the premiums or other costs associated with each option to cover a future potential LTC need. Compare the expected outlays with the expected retirement budget and financial resources.
- **Coverage:** Evaluate the scope of coverage each option offers, including what qualifies as long-term care services and the specific benefits available. Ensure the policy or product clearly defines the types of care covered, such as in-home care, assisted living, or nursing home care.
- **Eligibility:** Review the specific eligibility requirements for each option, whether government assistance programs with income and asset thresholds or private insurance policies that may require underwriting based on your health status. Understanding these criteria early can help determine which options are accessible and realistic for your long-term care planning.
- **Flexibility:** Consider each option's level of control and adaptability over your financial decisions. Some hybrid insurance products, such as those combining life insurance or annuities with long-term care benefits, offer more flexibility in how and when funds can be used. Additionally, determine whether the hybrid policy meets the criteria as a qualified

long-term care policy, which can provide significant tax advantages. Qualified policies may allow for the deductibility of premiums and tax-free withdrawals for long-term care expenses, enhancing both financial efficiency and care coverage. However, it's essential to verify the specific tax benefits available for each option based on IRS guidelines and your financial situation.

- **Risk:** Assess the potential risks associated with each option. For example, insurance policies may have the risk of premium increases over time, investment-based products could be subject to market performance, and long-term care may not be needed, leaving some benefits unused.
- **Discuss future needs with family:** Have open conversations with your family about long-term care's potential impact on your financial and personal lives. Collaborate on strategies to mitigate the burden, ensuring you avoid relying too heavily on any one family member for caregiving, and explore professional care solutions that align with your preferences and needs.
- **Work with a knowledgeable financial professional:** Selecting the best option for funding long-term care requires carefully considering personal needs and financial circumstances. Consulting with a financial professional specializing in retirement planning and long-term care strategies is highly beneficial for retirees and those nearing retirement. An experienced team of advisors can help navigate the complexities of various options, from traditional long-term care insurance to hybrid products and government programs, ensuring that decisions are aligned with your goals and preferences. They can analyze your situation, evaluate the costs and benefits of each approach, and provide personalized recommendations to help you make an informed, confident choice that maximizes both coverage and financial efficiency.



¹<https://www.genworth.com/aging-and-you/finances/cost-of-care>

²<https://crsreports.congress.gov/product/pdf/IF/IF10343>

³<https://www.medicare.gov/coverage/long-term-care>

⁴<https://www.medicare.gov/coverage/skilled-nursing-facility-care>

⁵<https://www.medicare.gov/coverage/home-health-services>

⁶<https://www.medicare.gov/coverage/hospice-care>

⁷<https://www.genworth.com/aging-and-you/finances/cost-of-care/cost-of-care-trends-and-insights>

⁸<https://pro.genworth.com/riiproweb/productinfo/pdf/131168.pdf>

⁹<https://www.va.gov/health-care/about-va-health-benefits/long-term-care/>

¹⁰<https://www.healthcare.gov/glossary/health-savings-account-hsa/>

¹¹<https://www.aarp.org/caregiving/financial-legal/info-2023/unpaid-caregivers-provide-billions-in-care.html#>

¹²<https://www.irs.gov/pub/irs-regis/10933397.pdf>

¹³<https://www.irs.gov/pub/irs-drop/rp-24-40.pdf>

¹⁴https://www.irs.gov/publications/p525#en_US_2023_publink1000229328 Long-Term Care Insurance Contracts

¹⁵<https://www.congress.gov/bills/109th-congress/house-bill/4/text/Sec.844>. Treatment of Annuity and Life Insurance Contracts with a Long-Term Care Insurance Feature.