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Financial Planners Risk Lawsuits for Failing to Recommend Realistic Plans for Long-Term Care

by Harley Gordon, J.D.

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Executive Summary

- Increased life expectancy is creating a greater need for long-term care planning. Yet many financial planners are failing to adequately discuss the issue with clients. Even planners who think they've adequately addressed the issue just by bringing up long-term care insurance to clients may find themselves vulnerable to a lawsuit.
- Many planners don't understand what long-term care is: a continuum of care, housing, and services needed when the aging process begins to exact a toll on our cognitive and physical abilities. It is custodial care, not skilled care, and thus is not paid for by most government programs.
- Planners and clients forget that it is the caregivers who must struggle to provide the care necessary to keep their loved one in the community, through either their unpaid labor or their financial assistance, or both.
- The need for long-term care insurance should be couched in terms of protecting the overall retirement plan, not merely as a way to protect assets. LTCI should be part of the establishment of a plan for providing long-term care.
- Trying to scare clients into buying LTCI—and having them sign a waiver if they don't buy it—will not necessarily insulate a planner from a lawsuit.
- The mere sale of LTCI to a client does not eliminate liability, because the version of the product sold may be inadequate.
- Following the recommendation of an attorney who says a three-year benefit combined with Medicaid planning is adequate will not eliminate liability.

Sheila Adams (not her real name) is a seasoned financial planner with a major Midwest insurance company. She is also one of its top producers. Like a growing number of professionals, she takes the subject of long-term care seriously and talks about its consequences with clients. But apparently, talking about it may not be enough.

Adams received a call from a good client's son, a local attorney. He proceeded to tell her that his dad was in a nursing home and paying for it with his life savings. He then told her, "You have 15 minutes to produce evidence that you recommended a long-term care plan in general and long-term care insurance in particular." Fortunately, she had discussed the matter and had a letter recommending the sale of long-term care insurance. Without it, she believes she would have been sued.

Long Life Is a Near Certainty, Planning for It a Necessity

A July 14, 2003, article in *USA Today*, "Insurers Adjust to Aging US Population," sums up why financial planners are talking to their clients about the need to adjust the payout of retirement portfolios. The article reported:

- Life insurance rates for Americans age 70 and older have dropped between 5 percent and 20 percent in the past few years
- By 2035 this group will more than double to 57 million
- The fastest-growing segment of the U.S. population is age 85 and older
- Insurers count family history far less if people reach age 70 because illnesses that killed their parents are far less likely to kill the insured

Advances in medicine are now taken for granted. Every day brings new treatments for illnesses once considered deadly. A June 6, 2003, story in the *Boston Globe* only confirmed what many believe: cancer will be cured in their lifetime. "Advances Begin to Tame Cancer" reported:

- Rapid advances in diagnosing and treating cancer have dramatically increased life expectancy
- This is particularly true with deadlier forms such as pancreatic and brain cancer
- By the year 2015, cancer will be classified as a chronic illness manageable with new classes of drugs

A reasonable corollary to this data is that an increased life expectancy creates a need for more services as the aging process takes its toll in the form of chronic debilitating diseases such as dementia, chronic obstructive pulmonary disease, crippling arthritis, and congestive heart failure. Yet many financial planners fail to discuss with clients the impact providing such care will have on their relationship with family members and family finances. Such failure exposes a fundamental risk to planners' reputation as professionals.

Need for Long-Term Care Must Be Discussed

Many financial planners fail to engage in a formal discussion of the impact long-term care has on a family because they do not fundamentally understand what long-term care is. Long-term care is a continuum of care, housing, and services needed when the aging process begins to exact a toll on our cognitive and physical abilities. It requires almost exclusively custodial care, not skilled care. Custodial care is defined as assistance with a person's activities of daily living (toileting, bathing, dressing, eating, transferring, and continence) or supervision necessitated by a severe cognitive impairment. Skilled care is medical in nature, requiring a plan of care created by a doctor for the treatment of complex medical issues and executed by a skilled nursing staff.

Ironically, it is not the afflicted who suffers but rather the caregivers. The patient will be taken care of by his or her family, which struggles to provide the care necessary to keep their loved one in the community. This effort exacts a terrible price on the caregiver's health (typically a daughter) and relationships with other family members, usually those siblings who do not share the burden. Anyone doubting this assessment need only ask someone who has been through it.

Understanding this essential fact is the first step in creating the confidence to bring the subject up in the ordinary course of creating a retirement plan. It allows the financial planner to ask the right questions, the most basic being "Have you thought about the consequences living a long life will have on your family?"

Financing Long-Term Care Critical in Any Retirement Plan

Long-term care is financed primarily by the family in the form of unpaid labor referred to as informal care. Formal care that is provided by trained professionals, including home health aids, and facility care such as assisted living and skilled nursing home care, is expensive. If financial planners do not recommend long-term care insurance (LTCI), the client is forced to rely on either a government program such as Medicare, Medicaid, or the Veterans Administration, or must ultimately reallocate retirement income and assets. A brief analysis of these programs indicates they are not the solution financial planners or clients think they are.

Medicare is the primary health care system for those 65 or older. It pays for skilled or rehabilitative care. Although never intended to do so, the program routinely paid for custodial care before 1998. Businesses such as home health care providers figured how to bill for services by making a custodial-care patient look like he or she needed skilled or rehabilitative care. Medicare put an end to it with the passage of the Balanced Budget Act of 1998 by replacing fee for service (which encouraged abuses) with a flat fee. Medicare was essentially returned to its roots of paying for medical, not custodial, care.

Medicaid is a federal and state partnership based on financial need. Originally designed for the poor and near-poor, it was appropriated by middle-class families looking for a way to avoid bankruptcy caused by the high cost of nursing home care. So-called *Medicaid planning* practiced by elder-law attorneys grew into an immensely popular field. Its impact on federal and state Medicaid programs has been such that in recent years there has been a concerted effort to shut down loopholes allowing Medicaid planning.

Medicaid planning is simply the process of taking assets that would have to be spent on care and transferring them out of the individual's name. Even when the attorney qualifies the client for benefits, Medicaid is far from free, a fact not often discussed by unskilled lawyers:

- Most families have qualified or low-basis assets. Transferring them creates serious tax issues.
- For couples, Medicaid planning can accomplish the goal of qualifying a spouse for benefits but the cost is high. Transferring qualified funds between the two creates an immediate tax, as well as the fact that once on benefits, the spouse in the community usually forfeits the majority of the institutionalized spouse's income.

Then there is the issue of where the client wants care. No one wants to go to a nursing home. Yet Medicaid planning accomplishes only one thing: qualifying the individual for payment in a nursing home. Medicaid pays little or nothing for home care, adult day care, and assisted living.

Veterans often cite the VA as a source of funding for custodial care. It is not. The VA may pay for care, but only in limited situations and it usually requires a financial contribution. In fact, the federal government has stated as much by encouraging active and retired military personnel to buy LTCI through the Federal Long-Term Care Insurance programs created by MetLife and John Hancock.

That leaves cash or long-term care insurance as the only viable solution to the financing of long-term care.

LTCI Seen as a Problem, Not a Solution

Put directly, I have found that many financial planners have a problem with long-term care insurance. Historically, the long-term care insurance industry has focused on selling product rather then selling a plan for long-term care. This puts it squarely at odds with financial planners who make their living selling a plan to protect the client's family and assets. Those plans range from estate preservation and business succession to basic wealth creation for young couples.

Every professional designation from the CFP certification to CLU reinforces this basic principle of professional conduct by teaching how to ask the right questions and work with other professionals such as estate planning attorneys and CPAs to draft the right plan. Although financial planners are certainly subject to malpractice claims, it is less likely that these claims will revolve around failure to establish and fund a plan.

If a financial planner does not understand the subject of long-term care, he or she cannot ask the right questions. Asking the right questions would lead to a discussion of the consequences of not having a plan rather than focusing on risk coverage. In turn, this should lead to the establishment of a plan for providing care. Such a plan probably will need to be protected by insurance. Unfortunately, long-term care insurance is often treated in a fashion similar to the selling of life insurance. It is usually in the context of suggesting LTCI as a way of protecting assets instead of a way of protecting a plan from long-term care expenses. This emphasis on protecting assets creates potential liability.

Professional Liability for Breach of Due Diligence

Due diligence: "The care that a reasonable person exercises under the circumstances to avoid harm to other persons or their property."

Merriam-Webster's Collegiate Dictionary

There are six areas where financial planners face potential liability regarding long-term care:

1. Failure to talk about a plan for long-term care as part of a financial retirement plan
2. Simply selling long-term care insurance (LTCI) disconnected from a plan for long-term care
3. Selling the wrong type of policy and amount of coverage
4. Selling the wrong carrier: Will the company be in business when it comes time to pay the claim? Does the company have a history of premium increases?
5. Failing to talk about the subject with wealthy clients and suggesting they can self-insure the cost
6. Not reviewing existing policies carefully for proper application to the client

When a Client Doesn't Buy LTCI

I talked with the prospect about LTCI and he didn't buy it. I even had him sign a waiver. How can I be held liable? The initial review of a case for an attorney specializing in professional liability focuses on determining what, if any, responsibility a financial planner has to a client, and then deciding whether it was breached. It is reasonable to assume that if producers are talking about the risks of needing long-term care as part of their presentation on selling LTCI, they are holding themselves out as a specialist. That would appear to establish a threshold of responsibility to use due diligence in protecting the interests of the prospect.

The liability arises when the producer focuses only on making the sale and doing so by scaring the prospect into submission with numbers and charts that talk about impending doom. If a policy is not sold and the individual needs care, the family (that is, children) can argue that the producer never discussed the family and financial consequences inherent in needing long-term care. In other words, the presentation was about selling a product, not working with the individual to establish a plan.

The lawyer most likely can brush aside the waiver of liability by arguing that its intent was not to absolve the producer of liability but rather as a sales gimmick to embarrass the person into buying the product.

When a Client Buys LTCI

My client bought LTCI based on my recommendations. How can I be held liable? Simply selling LTCI is not enough. For example, I have seen far too many policies with a $50-a-day benefit. What is that amount going to cover? The risk of diverting income and invading principal otherwise allocated for retirement is nearly certain should the person need long-term care. Worse, if the individual needs skilled nursing home care, he or she may actually qualify for Medicaid. Part of the patient-paid amount would be the daily benefit. Imagine the anger children have when they find…

- The benefit didn't prevent invasion of principal. This could mean that the children may have to help subsidize their parents. This also has an impact on the children's inheritance.
- The parent may qualify for Medicaid, which means the policy benefit paid for all these years is now going to the state to reduce its exposure.

Another example: A financial planner recommends a three-year benefit based on the concern that the cost of a lifetime benefit may kill the sale. The client goes on claim and exhausts the policy. The client now invades principal, most of which is qualified funds to pay for the cost of care. Federal taxes on lump-sum distributions run as high as 35 percent (plus state income tax).

The family argues that the producer should have considered the tax consequences of cashing in qualified funds. Had the producer done so, it would have become obvious to the insured that a lifetime benefit was the appropriate recommendation. The producer is accused of breaching his responsibility to exercise due diligence in protecting the financial interests of his client.

Recommending Against LTCI

I read in Consumer Reports *that my client doesn't need LTCI if he has more than $1.5 million.* It's puzzling when seasoned financial planners do not recommend LTCI to wealthy clients, but will usually go out of their way to recommend a Medicare supplemental policy to the same clients. Think about that for a moment: the client is paying $2,000 a year to cover perhaps $10,000 worth of exposure. Compare that with the expenses associated with needing long-term care.

The issue that will be raised by the children is not that the parent had enough to pay for care, but rather, why did the parent have to use his or her funds at all?

LTCI and Medicaid

I work with an attorney who believes that for families with modest estates, an LTCI policy with a three-year benefit combined with Medicaid makes financial sense. Where is the liability? At first glance this strategy makes sense. The attorney seemingly believes in the product, but suggests that because of the limited estate (usually under $300,000) and high cost of LTCI, only a three-year benefit is adequate.

A closer look reveals that the attorney believes in Medicaid planning with the intent of using LTCI as "bridge financing" to the program. That philosophy can have disastrous effects for the financial planner. Here's how it works: Medicaid will pay for custodial care in a skilled nursing home. The state has the right to look back three years from the date an application for benefits is submitted (five years if there is a transfer into or out of a trust). The thinking, therefore, is that as long as three years expire from the date of gifting, thereafter Medicaid will pay for the cost of care.

Example: Susan transfers $600,000 on February 1, 2004. She will qualify for benefits on February 1, 2007. The attorney therefore recommends a three-year benefit. He tells the client to gift everything the day she gets sick. The policy covers the next three years of care. When it runs out, Medicaid will pay.

The problem: The advice is based on a fundamental misunderstanding of long-term care and the tax code:

1. Most clients have qualified funds. By definition the three-year look-back begins only on the date assets are gifted. Result: Instant tax.
2. Many clients have low-basis assets. Gifting them transfers that basis. Result: A 15 percent tax on the capital gain when the children sell the assets.
3. The attorney assumes the client will need nursing home care when the policy runs out. What if he or she doesn't? Medicaid pays almost exclusively for nursing home care, not home care, adult day care, or assisted living. Families will do almost anything to keep their parents out of a nursing home. The only choice left is to make a nursing home placement, thus having Medicaid pay or re-transfer the funds back in order to pay for one of the other options not covered by Medicaid. There is little doubt that you and the attorney may have to answer to the family when the transfer is made. The error is compounded by the children paying privately as they continue to keep their parent at home.

The Solution Is in the Plan

Simply raising the issue of needing long-term care, as mentioned earlier, is not the solution. The answer lies in recognizing that long-term care planning requires the same commitment financial planners make to financial and estate planning.

This includes a thorough understanding of elder care issues, elder law, and care resources. It requires in-depth knowledge of what finances long-term care, with particular attention paid to the Medicare and Medicaid programs—resources clients often believe will provide funding. Without the facts, financial planners will continue to be reluctant to discuss the subject of long-term care for fear of encountering objections they cannot deal with confidently. Understanding the business of long-term care allows…

1. The right questions to be asked, which leads to…
2. Entering a discussion based on commonly held beliefs, such as that clients absolutely believe they will live a long life. They tell financial planners as much every time they ask for reassurance that their principal will remain intact after retirement. Establishing this baseline leads to…
3. A discussion of the effects long-term care has on a family and the client's best-thought-out retirement plan. In turn this leads to…
4. The establishment of a plan for providing care. It includes having the client think about who will provide care and where it will be delivered; this leads to…
5. A discussion of how the plan will be paid for. This allows the financial plan-

ner to talk about the impact of needing care on the client's retirement plan. Included is a discussion of how the plan allocates income and assets for retirement, not for long-term care. Because no federal program will pay for custodial care, the client is forced to rely on self-funding, resulting in the possibility that he or she may have to invade principal.

Long-Term Care Insurance

The subject of long-term care insurance has been purposely left for the end of this article precisely because it is so often talked about at the beginning of articles on long-term care. It is raised in the context of protecting assets, giving people choices, and not being a burden—not in the context of protecting a plan. The early presentation is product-driven, rather than advice-driven, and based on frightening people into submission.

The facts, however, are different. Long-term care insurance is a professional tool that, used correctly, can protect a family from the devastating cost of providing care. It is a complex product that few consumers understand. How does the average consumer know what daily benefit to buy and for how long? How many understand the difference between reimbursement, cash, and indemnity payments? Do they buy a joint policy or a shared benefit policy? The complexity of the product creates the perfect opportunity for financial planners to craft the right benefits to protect the long-term care plan they drafted.

Conclusion

Before making the commitment to suggest long-term care insurance, financial professionals are advised to make the commitment to understand long-term care. Once the professional feels comfortable discussing the subject, it is more likely he or she will integrate it into a retirement plan. As with all plans, insurance is a critical component in making sure it executes properly.

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Posted with permission from the *Journal of Financial Planning*/September 2005