

# Who Will Pay for the Baby Boomers' Long-Term Care Needs?

## Expanding the Role of Long-Term Care Insurance

Janemarie Mulvey, Ph.D.

Barbara Stucki, Ph.D.

April 1998

RESEARCH  
FINDINGS



*Order copies of this Research Finding from the  
American Council of Life Insurance by calling 202-624-2372.  
Refer to inventory number 7358001.*

Copyright 1998  
The American Council of Life Insurance  
Washington, D.C.

# Contents

|   |    |
|---|----|
| Overview .....  | 1  |
| The Looming Crisis: Aging Baby Boomers .....  | 3  |
| Long-Term Care Expenditures Are Likely<br>to Increase Dramatically? .....               | 5  |
| The Impact of Rising Long-Term Care Expenditures<br>on Government and Individuals ..... | 7  |
| Private Insurance Offers a Solution<br>to the Looming Long-Term Care Crisis .....       | 9  |
| Realizing the Potential of Private<br>Long-Term Care Insurance .....                    | 11 |
| Conclusion .....  | 15 |

## **Illustrations**

### ***Figures***

|          |  |    |
|----------|--|----|
| Figure 1 | Growth of Elderly Population, 1990–2030 .....                              | 3  |
| Figure 2 | Nursing Home Population, by Age, 2000–2030 .....                           | 5  |
| Figure 3 | Total Nursing Home Expenditures, 2000–2030 .....                           | 6  |
| Figure 4 | Medicaid Nursing Home Expenditures, 2000–2030 .....                        | 7  |
| Figure 5 | Medicaid Nursing Home Costs:<br>Revenues Vs. Expenditures, 2000–2030 ..... | 8  |
| Figure 6 | Out-of-Pocket Costs for Nursing Home<br>Services, 2000–2030 .....          | 8  |
| Figure 7 | Financing Nursing Home Expenses in Year 2030:<br>Two Scenarios .....       | 9  |
| Figure 8 | Impact of Long-Term Care Insurance<br>on Medicaid Expenditures .....       | 10 |
| Figure 9 | Impact of Long-Term Care Insurance<br>on Out-of-Pocket Expenditures .....  | 10 |

### ***Tables***

|         |  |    |
|---------|--|----|
| Table 1 | Ways to Pay for Future Long-Term Care .....                | 13 |
| Table 2 | Long-term Care Insurance:<br>Average Annual Premiums ..... | 14 |
| Table 3 | Who Can Afford Long-term Care Insurance? .....             | 14 |

---



## Overview

**I**n 1998, the American Council of Life Insurance conducted a study to assess the resources that will be required to meet the long-term care needs of aging baby boomers. While it was clear that this large segment of the population will accelerate the demand for long-term care in the 21st century, the potential financial impact on government programs and individuals that will provide care to boomers remains uncertain. The purpose of this study was twofold. First, ACLI examined the future long-term care costs of the baby boomers. Our study projected long-term care expenditures to the year 2030, when the last of the baby boomers turns age 65. We then determined the subsequent effects of these needs on Medicaid expenditures and on individuals' out-of-pocket costs. Second, we sought to measure to what extent private long-term care insurance could alleviate both the personal and societal burden of paying for long-term care, especially when provided in the most expensive setting, nursing homes.

The study findings were dramatic. In the next 30 years, total nursing home expenditures paid by Medicaid are expected to increase 360 percent to \$134 billion (all costs are reported in 1996 dollars to adjust for inflation). In addition, if current trends continue, costs paid directly by individuals ("out of pocket") for nursing home care will increase from an estimated \$33 billion in 2000 to \$158 billion by 2030. This represents a 378 percent increase in total out-of-pocket costs for nursing home care.

There is still time to seek out private-sector solutions to the looming long-term care crisis. This study shows that private insurance can go a long way toward financing the

*There is still time to seek out private-sector solutions to the looming long-term care crisis. This study shows that private insurance can go a long way toward financing the baby boomers' long-term care needs.*

---

baby boomers' long-term care needs. If a large number of baby boomers purchased long-term care insurance, the share of nursing home expenditures paid by private insurance could increase from 3 percent today to 29 percent in 2030. Under this scenario, the Medicaid program could save \$28 billion, or 21 percent, of total Medicaid nursing home expenditures. These savings translate into 19 percent fewer nursing home residents who would need to rely on Medicaid in 2030.

About 40 percent of out-of-pocket costs could be saved by the increased ownership of long-term care insurance. Total out-of-pocket expenditures could be reduced by \$63 billion to \$95 billion in 2030. Our projections also suggest that 385,000 of the 863,000 nursing home residents at risk of impoverishment in 2030 could avoid reliance on Medicaid through private insurance. This means that long-term care insurance could reduce the number of nursing home residents who "spend down" their assets by 44 percent.

The potential of private insurance to finance future long-term care costs will depend on three factors. The first is the extent to which baby boomers plan ahead for long-term care needs. This will present a significant challenge, since many Americans underestimate the risk of becoming disabled and have misconceptions about who will pay for long-term care. These will need to be addressed by educating baby boomers about:

- ◆ The limitations of government programs in paying for long-term care services.
- ◆ The potential risk of needing long-term care services.

A second part of the solution lies in raising the awareness that rapid increases in long-term care expenditures projected for the 21st century can have serious implications for baby-boomers' retirement security. By 2030, an unanticipated nursing home stay (projected to cost \$97,000 a year in constant 1996 dollars)<sup>1</sup> could deplete hard-earned savings and threaten a family's financial protection. To avoid impoverishment, baby boomers need to incorporate long-term care insurance as an essential part of retirement planning.

The third key to realizing the potential of private insurance is encouraging baby boomers to purchase insurance at younger ages. Generally, premiums are much lower when purchased before age 65. For example, compared to the costs for a 65-year-old, premiums are more than 50 percent lower for a 55-year-old, and 70 percent lower for a 45-year-old. The results of this study indicate that over 80 percent of individuals ages 45 to 49 could afford a long-term care policy.

### WHAT IS LONG-TERM CARE?

Long-term care consists of many different services aimed at helping people with chronic conditions. Those who need help at home with everyday activities may rely on personal assistance services or a homemaker. Care in the community includes adult day-care services and assisted living facilities. Individuals who need skilled care or constant supervision often receive care in a nursing home.

Long-term care can be expensive. For example, a person with a severe disability who lives at home may pay over \$36,000 per year for the help of a home care aide.<sup>2</sup> Assisted living facilities charge \$26,000 on average.<sup>3</sup> A nursing home can cost \$40,000 per year.<sup>4</sup> (These figures vary widely depending on geographic location.)

---

# The Looming Crisis: Aging Baby Boomers

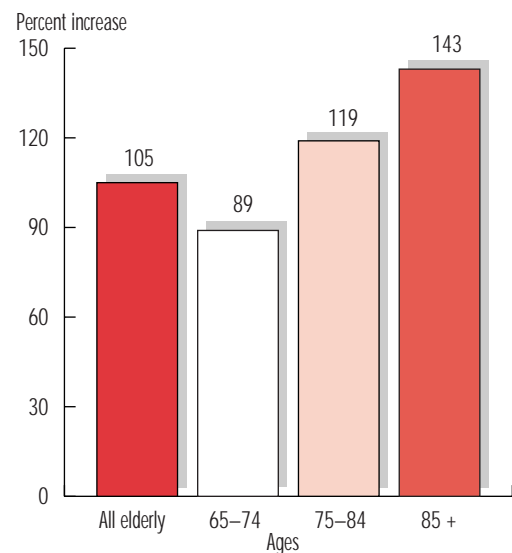
One of the biggest challenges facing America in the 21st century will be the aging of the “baby boomers”— individuals born between 1946 and 1964. Because baby boomers represent a large segment of the population, at each stage of their lives they have dramatically affected societal trends and the demand for services. In their formative years, they crowded the school systems. As they reached adulthood, they dominated the housing and labor markets. Now as they begin to save for retirement, the stock market is reaching record highs.

Baby boomers’ impact on economic and social trends will continue to be felt as members of this large and influential group ages. The first baby boomers have already turned 50. As the 21st century approaches, over 70 million baby boomers will face the prospect of retirement and the needs associated with aging. These demographic realities will present new challenges to families and to society. By the year 2030, when the last of the baby boomers reaches retirement, the number of elderly individuals is estimated to double from 35 million to nearly 70 million. More than 20 percent of the population will be over age 65 compared to 13 percent in 1990.<sup>5</sup> This means that in about 30 years, the demographics of 32 states will resemble those of Florida today.

Life expectancy also is expected to improve. As a result, individuals ages 85 and older will be the fastest-growing segment of the elderly population, increasing 143 percent between 1990 and 2030 (Figure 1).

What will happen as the baby boomers enter retirement? How will their needs affect the cost of health care, particularly long-term care? Although there are still many uncertainties regarding the future of this diverse group, it is clear that the boomers will play an increasingly important role in our long-term care system.

Figure 1  
**Growth of Elderly Population,  
1990–2030**



Source: Social Security Administration



---

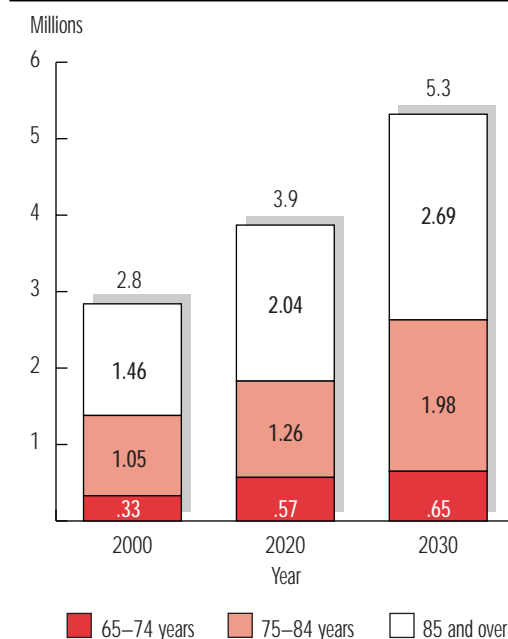
# Long-Term Care Expenditures Are Likely to Increase Dramatically

**I**t is not clear whether increased longevity will bring more healthy years for aging baby boomers or additional years limited by chronic conditions. Currently, people 85 and older are almost six times as likely to need long-term care than people in their 60s.<sup>6</sup> While some researchers suggest that medical breakthroughs will reduce the incidence of disability, others maintain that raising life expectancy may well increase the likelihood of developing age-related disabilities, such as Alzheimer's disease. Although there are still many uncertainties regarding the likelihood of becoming disabled in the future, unprecedented growth in the elderly population by 2030 alone will place additional burdens on the long-term care system.

Increasing numbers of baby boomers are becoming aware of long-term care as they help their own aging parents. Many of these caregivers are beginning to wonder, who is going to take care of them? Typically baby boomers emphasize that they do not want to end up in nursing homes. However, despite preferences for services to help people stay in the home and community, public programs pay predominantly for institutional care. Medicaid, the largest government payer of long-term care, devotes only 21 percent of its long-term care expenditures to cover home and community-based services.<sup>7</sup> Less than half of the states (22) have programs that pay for long-term care services in assisted living facilities.<sup>8</sup> As a result, individuals who impoverish themselves by paying for long-term care (because they lack private insurance or substantial funds) could spend their remaining days as a Medicaid recipient in a nursing home.

Given the current institutional bias in how long-term care services are financed and in the absence of a major change, nursing homes will continue to dominate long-term care expenditures over the next 30 years. Under this scenario, by 2030 we can expect the number of people receiving institutional care to increase to 5.3 million individuals, almost double the current nursing home population (Figure 2).

Figure 2  
**Nursing Home Population, by Age, 2000–2030**

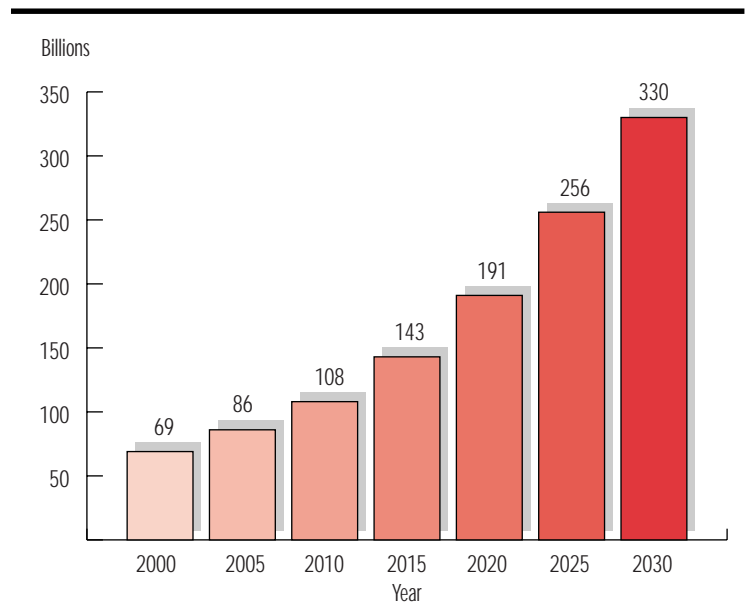


Source: American Council of Life Insurance

Not only will the total number of nursing home residents increase but so will the costs per resident. Since 1990, the costs per stay have increased at an annual average rate of 3 percent above the overall rate of inflation. Assuming this trend continues, the annual cost of a nursing home stay will increase from \$40,000 today to \$97,000 by 2030.

The rise in the numbers of nursing home residents, combined with a higher cost per stay, will lead to a quadrupling of nursing home expenditures; by the year 2030, total expenditures for nursing home care could reach \$330 billion (Figure 3). To put this number into perspective, nursing home expenditures in 2030 will equal the size of the entire Social Security budget today.

Figure 3  
**Total Nursing Home Expenditures,  
2000–2030<sup>a</sup>**



<sup>a</sup> Projections adjusted for inflation.

Source: American Council of Life Insurance

---

# The Impact of Rising Long-Term Care Expenditures on Government and Individuals

**R**ising numbers of nursing home residents will increasingly burden the Medicaid program. Currently, Medicaid pays about 41 percent of total nursing home expenditures.<sup>9</sup> Assuming Medicaid's share of total expenditures remains constant, the aging of the population alone will lead to a doubling of nursing home residents who receive Medicaid assistance. Total nursing home expenditures paid by Medicaid also are expected to increase 360 percent by 2030, to \$134 billion (Figure 4).

These trends will be unsustainable at current tax rates. Legislation to increase taxes dramatically to fund the expected in-

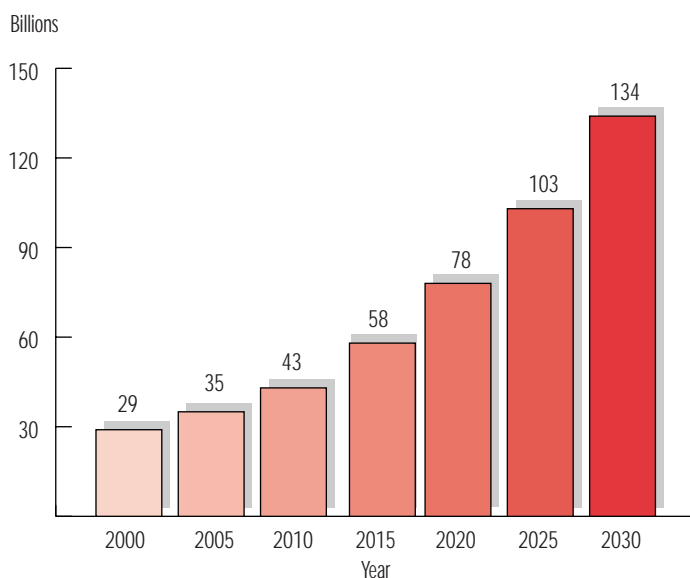
creases in Medicaid is unlikely in an era of balanced budgets and fiscal conservatism. Yet, without explicit increases in tax rates, future growth in tax revenues to fund Medicaid will be limited to the growth in overall wages. Consequently, Medicaid nursing home spending is almost certain to outpace growth in tax revenues over the next 30 years (Figure 5). And, without additional tax revenues, Congress will be forced to limit Medicaid nursing home expenditures—either by reducing benefit levels or restricting eligibility requirements. Such actions could threaten the safety net for low-income individuals who have no alternatives.

To control Medicaid expenditures, some states are emphasizing home and community-based care. While less costly per person than institutional care, research studies are not conclusive as to whether any savings would be offset by increased demand for services.<sup>10</sup> Other strategies involve limiting provider fees, curtailing growth in nursing home beds, and using “care management.” It is still unclear whether these approaches will contain future long-term care costs.

Should baby boomers fail to plan ahead, and neglect to purchase private insurance, much of the burden of rising nursing home costs will continue to fall on individuals and their families. Currently, almost half (48 percent) of nurs-

Figure 4

## Medicaid Nursing Home Expenditures, 2000–2030<sup>a</sup>



<sup>a</sup> Projections adjusted for inflation.

Source: American Council of Life Insurance

ing home costs are paid out of pocket by individuals.<sup>11</sup> If this trend continues, projected out-of-pocket expenditures for nursing home care will increase from an estimated \$33 billion in 2000 to \$158 billion in 2030 (Figure 6). This represents a 378 percent increase in total out-of-pocket costs for nursing home care by 2030.

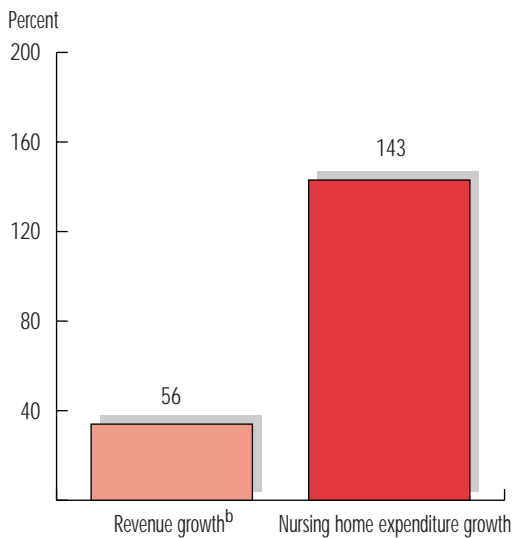
Out-of-pocket payments for long-term care services are substantial, but do not capture the full cost of caring for older people who have physical or mental limitations. About 57 percent of frail elders who live in the community rely solely on family and friends for care.<sup>12</sup> In fact, a recent survey found that 22 million American households have at least one member providing some unpaid assistance to a spouse, relative or other person older than 50.<sup>13</sup> Whether family caregivers will be able to continue offering this level of help to numerous, very old relatives remains to be seen.

Rising life expectancy increases the likelihood that aging baby boomers will rely more on their children for help. As boomers live longer, they also are more likely to face multiple chronic conditions that require complex and physically demanding care. At the same time, smaller families and greater geographic dispersion are shrinking the pool of potential family caregivers. Caregiving in the 21st century will be further complicated by the increasing reliance on family members who are employed. In 1960, only one-third of married women worked outside the home.<sup>14</sup> By 1996 over three-fifths of women were in the labor force. About 64 percent of family caregivers are employed, most (54 percent) full time.<sup>15</sup> As the physical stress of caregiving increases, many of these families may face additional financial burdens if they have to rely more on paid long-term care.

Equally troublesome is the growing number of Americans who may lack family support to help them if they become disabled. About 21 percent of baby boomers were childless in 1995.<sup>16</sup> Individuals without children available to provide assistance often require institutionalization at earlier ages than those with family support.

Figure 5

**Medicaid Nursing Home: Revenues Vs. Expenditures,<sup>a</sup> 2000–2030**



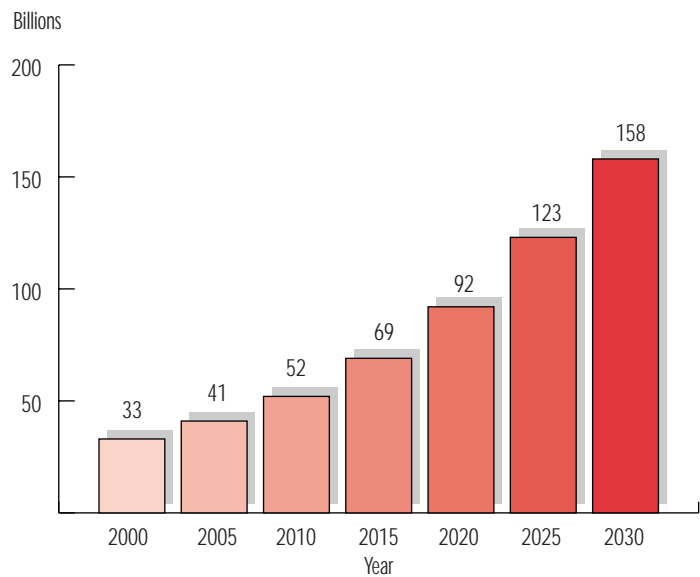
<sup>a</sup> Projections adjusted for inflation.

<sup>b</sup> Based on growth in taxable payroll as reported by the Social Security Administration.

Source: American Council of Life Insurance

Figure 6

**Out-of-Pocket Costs for Nursing Home Services, 2000–2030<sup>a</sup>**



<sup>a</sup> Projections adjusted for inflation.

Source: American Council of Life Insurance

# Private Insurance Offers a Solution to the Looming Long-Term Care Crisis

**A**s the baby boomers age, rising expenditures for Social Security and Medicare will leave little room for expanding public long-term care programs. In response to this scenario, the policy debate is shifting toward greater support for private-sector solutions to financing long-term care. The willingness of policymakers to support private-sector initiatives is evident in the recent enactment of the Health Insurance Portability and Accountability Act of 1996 (HIPAA). HIPAA allows individuals to deduct the cost of premiums for tax-qualified long-term care insurance as medical expenses from their federal taxes. HIPAA also excludes benefits paid by a qualified policy from taxable income. At the same time, this legislation signals that policymakers expect consumers to assume greater responsibility for financing their long-term care needs.

Can long-term care insurance help protect baby boomers from financial hardship and reduce their reliance on Med-

icaid? To answer this question, ACLI examined long-term care expenditures under two alternative financing scenarios:

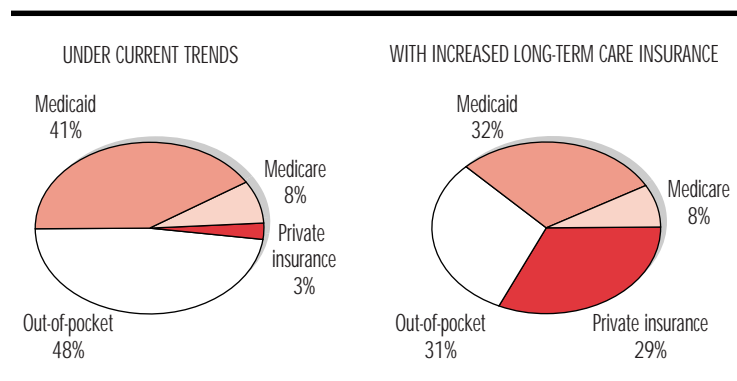
- ◆ Current financing trends continue.
- ◆ Purchases of long-term care insurance increase.

In the case of increased purchase of long-term care insurance, we assumed that everyone 35 and older in the year 2000 who could afford a policy purchased a policy.<sup>17</sup> Long-term care insurance policies incorporated coverage for either two or five years of benefits and included compound inflation protection of 5 percent a year. Individuals purchased the policy they were most able to afford.

We concluded that private insurance can be an important source of funding for long-term care in the future and can substantially reduce nursing home expenditures for individuals and Medicaid (Figure 7). Assuming that three-fourths of the purchasers retain their policies to the year 2030, the share of nursing home expenditures paid by private insurance increases from 3 percent today to 29 percent in 2030. At the same time, Medicaid's share of nursing home expenditures declines from 41 percent to 32 percent. Costs paid directly by individuals (out of pocket) could decline from 48 percent to 31 percent. Under this scenario,

Figure 7

## Financing Nursing Home Expenses in Year 2030: Two Scenarios



Source: American Council of Life Insurance

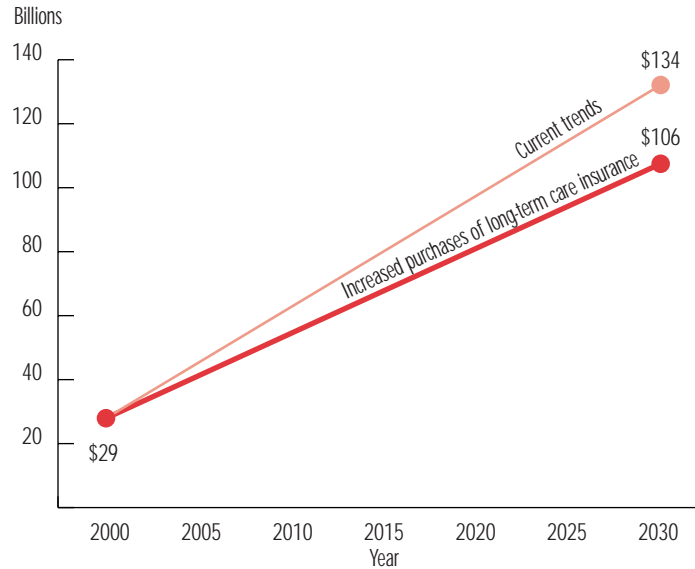
the proportion of national expenditures for nursing home care paid by private insurance (29 percent) would almost equal that of the Medicaid program (31 percent) and private out-of-pocket payments (30 percent).

The Medicaid program could save \$28 billion, or 21 percent, of total Medicaid nursing home expenditures as a result of increased ownership of long-term care insurance (Figure 8). This amount represents more than one out of every five dollars that Medicaid would have had to spend on nursing home care in the year 2030. These savings translate into 19 percent fewer nursing home residents who would need to rely on Medicaid in 2030—or about 490,000 individuals.

The loss of financial independence caused by impoverishment is a big concern to individuals who need long-term care. The projections suggest that 385,000 of the 863,000 nursing home residents at risk of impoverishment in 2030 could avoid reliance on Medicaid through private insurance. This means that long-term care insurance could reduce the number of nursing home residents who “spend down” by 44 percent. In addition, many people who enter a nursing home as a Medicaid recipient impoverished themselves paying for care in the community. A significant portion of these individuals may avoid institutionalization if their long-term care policy includes home care.

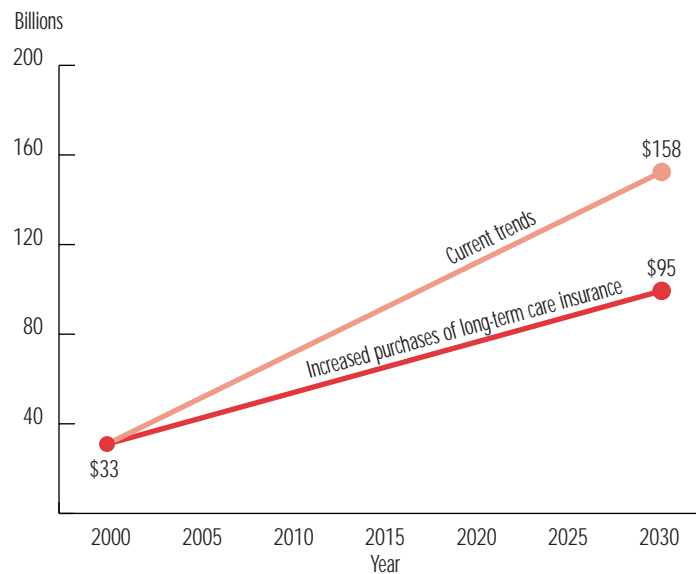
About 40 percent of out-of-pocket costs (borne by nursing home residents and their families) could be saved by the increased ownership of long-term care insurance. Total out-of-pocket expenditures could be reduced by \$63 billion, to \$95 billion, in 2030 (Figure 9).

Figure 8  
Impact of Long-Term Care Insurance on Medicaid Expenditures



Source: American Council of Life Insurance

Figure 9  
Impact of Long-Term Care Insurance on Out-of-Pocket Expenditures



Source: American Council of Life Insurance

---



# Realizing the Potential of Private Long-Term Care Insurance

**P**ivate long-term care insurance consists of a wide variety of products that help protect people if they need assistance due to a disability or chronic condition. Unlike government programs that focus primarily on institutional care, long-term care insurance policies cover a wide range of services to help people live at home, participate in community life, as well as receive skilled care in a nursing home. Policies also may include respite care, coverage for home modifications for the disabled, or payment for family caregivers. Most policies pay for services such as assisted living that are not covered under many state Medicaid programs. These options can enable the frail elderly to live in the community and retain their independence.

Private insurance currently pays for only a small portion of the nation's long-term care expenditures. Nevertheless, while the market for long-term care insurance is small, it is growing. Over 4.3 million policies had been sold as of 1995.<sup>18</sup> The small portion of long-term care costs paid by private insurance also reflects the fact that many who have purchased a policy have not yet begun to utilize long-term care services.

About 6 percent of elderly people and a very small number of baby boomers have purchased long-term care insurance. Limited sales among baby boomers may stem from widespread denial about the risk of needing long-term care. Having largely invented the culture of youth during the 1960s, many of the baby boomers are still concerned with

sustaining their youth and vitality. In addition, a large proportion of Americans continue to have numerous misconceptions about long-term care.

Whether private insurance will play a greater role financing the cost of long-term care in the next century also depends in large part on the extent to which baby boomers plan ahead for their retirement. To help encourage individuals to plan for their long-term care needs, it is essential to:

- ◆ Educate baby boomers about the limitations of federal and state programs that pay for long-term care.
- ◆ Increase awareness about the risk of needing long-term care and the impact of unplanned long-term care expenditures on financial security.
- ◆ Encourage baby boomers to incorporate long-term care insurance as an essential part of retirement planning.
- ◆ Encourage the purchase of long-term care insurance at younger ages when premiums are less expensive.

---

**Baby boomers need information about the limitations of government programs that pay for long-term care.**

Many Americans believe that Medicare will pay for their long-term care needs. In reality, this program primarily focuses on acute care needs (hospital stays and physician visits). The Medicare home health benefit is also medically oriented, and is targeted to people who need skilled nursing care and rehabilitative therapy at home. Medicare does not pay for help with daily activities unless provided with home health care. In addition, the nursing home benefit under Medicare only covers short stays (up to 100 days).

Those who are very poor can turn to Medicaid. In fact, unless the way long-term care is financed changes when baby boomers grow old, 68 percent of this generation who use a nursing home could depend on Medicaid.<sup>19</sup> Some of these will be individuals who are poor, while others will have experienced a drop in income, possibly because of the death of a spouse and a subsequent loss of the spouse's pension. In addition, without adequate private insurance, a significant number are likely to become poor paying for medical costs and for long-term care in the community.

Many baby boomers are unaware that the Medicaid program requires people with disabilities to impoverish themselves before they are eligible for public assistance. As a result, middle-income families have few options but to use their own income and assets to pay for their long-term care needs. In 2030, a nursing home stay will cost \$97,000 a year. This is likely to equal more than two and a half times the projected

median income of \$35,000 for elderly households in 2030.<sup>20</sup> These resources will be inadequate to pay for a single year of nursing home care.

**Baby boomers need to become aware of the risk of becoming disabled and the impact of unplanned long-term care expenditures on their financial security.**

Because old age seems so far off, few members of the baby boom generation have begun to prepare for their own long-term care needs. Part of this stems from the fact that Americans tend to underestimate the risk of disability. A recent survey reported that more than two-thirds of the survey respondents found it difficult to admit that they would ever need some long-term care during their lives.<sup>21</sup>

In reality, today about one in five Americans older than 65 and almost half of Americans 85 and older who live in the community require assistance with their everyday activities.<sup>22</sup> The risks of needing nursing home care also are substantial. Over half of women and nearly one-third of men 65 and older will stay in a nursing home sometime during their lifetime.<sup>23</sup>

As life expectancy—and the risk of disability—increases, retirement is becoming a less predictable stage in life. An unanticipated nursing home stay can deplete hard-earned savings and threaten a family's financial future. At the same time, the 21st century could see an erosion of the social safety net for aging baby boomers. If expenditures for long-term care continue to rise dramatically, federal and state governments may try to control costs by limiting Medicaid benefits and tightening eligibility requirements for middle-income individuals. At the same time, it will become increasingly challenging for the children of baby boomers to serve as caregivers to their parents and other relatives.

What this means is that baby boomers need to look at retirement security in different terms from their parents. Many fail to realize that rapid increases in long-term care expenditures projected for the 21st century have serious implications for their retirement security.

**Baby boomers need to incorporate long-term care insurance as an essential part of retirement planning.**

Many baby boomers are not planning for the future because they are preoccupied with more immediate concerns. Boomers currently represent almost half of all workers, and are parents of about 60 percent of the nation’s children under age 18.<sup>24</sup> Now in their high-expense years (ages from 34 to 52), boomers’ child care and housing expenses tend to dominate their budgets. In addition to immediate needs, baby boomers also are trying to save for their children’s college educations.

Public policy analysts speculate about the financial well-being of baby boomers, especially upon retirement. Some baby boomers could spend one-third of their lives in retirement. Looking into the future, there are two key goals of retirement security: 1) saving enough money for retirement, and 2) protecting against life’s uncertainties, including the uncertainty associated with future long-term care costs. While both goals require planning, the calculations are very different.

Table 1

**Ways To Pay for Future Long-Term Care**

|  | AGE TODAY |           |
|--|-----------|-----------|
|  | 45 years  | 60 years  |
| <b>OPTION 1—ASSET ACCUMULATION</b>                                       |           |           |
| Annual savings needed  | \$3, 557  | \$4,481   |
| Lifetime assets needed at age 85 to pay for 2 years of nursing home care | \$489,446 | \$235,432 |
| <b>OPTION 2—PURCHASE PRIVATE LONG-TERM CARE INSURANCE</b>                |           |           |
| Annual premium contributions   | \$417     | \$824     |
| Lifetime value of premiums   | \$57,907  | \$52,097  |
| <b>POTENTIAL SAVINGS FROM LONG-TERM CARE INSURANCE</b>                   |           |           |
| Annual savings from long-term care insurance                             | \$3,140   | \$3,657   |
| Lifetime savings from long-term care insurance                           | \$431,539 | \$183,335 |

Source: American Council of Life Insurance

Note: Author’s calculations are based on a 2-year long-term care policy with inflation protection of 5 percent. All numbers are represented in 2030 dollars and assume a 7 percent return.

Saving for retirement is largely a matter of accumulating enough assets to last a lengthy retirement period. There has been much debate on whether the baby boomers are saving enough. Some believe they are saving enough and others believe most boomers’ savings will fall short of their needs. While beyond the scope of this paper, the answer to this question ultimately will affect the baby boomers’ standard of living in retirement.

The need to protect against life’s uncertainties, specifically the risk of needing long-term care, requires a much different approach. This is because long-term care costs are extremely expensive, and paying for them requires a large amount of savings. For example, today’s 45-year-old, who will need nursing home care when she is 85 years old, will need \$489,000 (this includes the effects of inflation) for a two-year stay. To reach this goal she has to save \$3,500 annually. Considering the multiple demands on boomers today, relying on savings to pay for long-term care needs is not a financially feasible option.

Another alternative is long-term care insurance. Long-term care insurance makes it possible for middle-income families to manage the risk that they may become disabled without having to save large amounts of money each year. Long-term care insurance, like other insurance, is intended to spread the risk across many individuals and thus lower costs to any one individual in the event he or she needs long-term care services.

Today’s 45-year-old would only have to pay about \$417 a year for a long-term care policy that includes coverage for two years in a nursing home (with inflation protection of 5 percent a year). Long-term care insurance thus could save her \$3,140 a year in savings that could be used for many of her more

pressing needs, including accumulating assets for retirement. In terms of lifetime savings, these numbers are even more staggering. After paying her long-term care premiums, the 45-year-old woman could protect \$431,539 of her savings if she buys a long-term care policy instead of trying to pay for nursing home care on her own (Table 1).

**Baby boomers need to understand the importance of purchasing insurance at younger ages, when it is more affordable.**

Many policymakers have emphasized that the high cost of private long-term care insurance is unaffordable for most Americans. In reality, the cost of a long-term care insurance policy is tied to the age of purchase. Variations in premiums by age reflect the increased risk of needing long-term care as people grow older (Table 2). Insurance companies are able to assume the risk presented at older ages only if they charge higher premiums.

Consequently, the earlier policies that are purchased, the lower the premiums. Gener-

ally, premiums are much lower when purchased before age 65. For example, premiums are 70 percent lower for a 45-year-old as compared to those for a 65-year-old (\$702 per year at age 45 for a five-year policy with inflation protection). Similarly, premiums are 54 percent lower for a 55-year-old as compared to those for a 65-year-old (\$1,068 per year at age 45 for a five-year policy with inflation protection).

Indeed, about three-quarters of individuals ages 35 to 44 could afford a policy if they spend 2 percent or less of their income on private insurance (Table 3). Under this criteria, almost half (46 percent) of those ages 35 to 44 would be able to afford a five-year policy, while the rest could purchase a two-year policy. Similarly, 58 percent of individuals ages 45 to 49 could afford a five-year policy.

Purchasing at an earlier age has other benefits. Since this product involves medical underwriting, those who buy insurance at an early age are more likely to qualify for coverage. In addition, lower premiums increase the likelihood that baby boomers will be able to purchase policies with very comprehensive benefits. A recent study found that purchasers ages 55 to 64 on average have policies with more coverage (almost seven years) than older purchasers (about five years for those ages 65 to 74 and four years for those 75 and older).<sup>25</sup> In addition, younger purchasers are far more likely to choose inflation protection (61 percent) as a policy feature in contrast to older purchasers (38 percent of those ages 65 to 69, 27 percent of those ages 70 to 74).

Table 2

**Long-Term Care Insurance: Average Annual Premiums<sup>a</sup>**

| Ages  | 2-year policy | 5-year policy |
|-------|---------------|---------------|
| 35-39 | \$358         | \$507         |
| 40-44 | 403           | 605           |
| 45-49 | 500           | 734           |
| 50-54 | 645           | 905           |
| 55-59 | 892           | 1,204         |
| 60-64 | 1,265         | 1,709         |
| 65-69 | 1,849         | 2,432         |
| 70-74 | 2,638         | 3,610         |
| 75 +  | 3,851         | 5,274         |

Source: American Council of Life Insurance

<sup>a</sup> Premiums are a composite of five, large long-term care insurance companies. Actual prices may vary by company.

Table 3

**Who Can Afford Long-Term Care Insurance?**

| Ages  | Percent |
|-------|---------|
| 35-39 | 73      |
| 40-44 | 71      |
| 45-49 | 81      |
| 50-54 | 72      |
| 55-59 | 63      |
| 60-64 | 47      |
| 65 +  | 31      |
| Total | 62      |

Source: American Council of Life Insurance

---



## Conclusion

Projections about long-term care needs 30 years into the future may seem too distant for consumers and policymakers faced with immediate concerns. Nonetheless, this study provides an important framework within which to examine options to help Americans plan their long-term care needs. Long-term care insurance has the potential to significantly reduce future out-of-pocket and Medicaid expenditures for long-term care. If a large proportion of baby boomers purchased long-term care insurance, total nursing home expenditures paid by Medicaid could decline from the current 41 percent to 32 percent. In addition, the proportion of total nursing home expenditures paid by individuals out of pocket could decline from the current 48 percent to 31 percent.

Cost estimates presented here reflect only the tip of the iceberg. In 2030, baby boomers will be concentrated between ages 65 and 84. By 2050, however, all of the baby boomers will have reached age 85 (and beyond), and the probability of needing long-term care services will have increased markedly. By 2050, therefore, both long-term care costs, and the potential savings from long-term care insurance, could be considerably higher.

Our analysis assumes that in 2030 the process of “spending down” to become eligible for Medicaid would be similar to what it is today. We also assume that the share of nursing home costs paid by Medicaid (under our current financing trends scenario) would remain constant through 2030. In reality, many more middle-income baby boomers could be impoverished by nursing home costs and thus be eligible for Medicaid in the 21st century. Our projections show that nurs-

ing home costs are rising faster than overall inflation and incomes. In this case, increased purchase of long-term care insurance could provide even greater savings to Medicaid than this study suggests.

If the government is serious about encouraging people to purchase private insurance, it has to do more. Educational efforts should address the need for long-term care, the limitations of Medicaid and Medicare programs, and the advantages of purchasing long-term care insurance at younger ages. Tax incentives for long-term care insurance premiums could make policies more affordable for older individuals and those with modest incomes.

Baby boomers must be encouraged to plan. Private long-term care insurance is affordable for most Americans, especially if purchased at an early age. The insurance industry is offering innovative products that increase options for people with modest incomes. For example, individuals can obtain riders to their life insurance policies that help finance long-term care. Under these policies, the insurer pays a portion of a life insurance benefit to the policyholder instead of paying it as part of after-death benefits to a beneficiary. Also, more employers are participating in the long-term care insurance market, offering employees earlier and more affordable long-term care insurance.

## Methodology

ACLI needed a database that would: 1) simulate affordability of long term care insurance as well as 2) determine Medicaid eligibility with and without long-term care insurance. The March 1996 Current Population Survey (U.S. Department of Commerce) was used as the basis for this analysis. This database was further enhanced to include the asset holdings of the baby boomers using data from the Survey of Income and Program Participation (Bureau of the Census). Projections of income and asset growth for the baby boomers were derived from Lewin-VHI.<sup>26</sup>

Information on financing of nursing home expenditures under current financing trends was based on estimates by the Brookings ICF model and published in Weiner, et al. (1994). (See endnote 9.) However, because his data does not capture the recent growth in private insurance, we simulated the impact of current ownership trends on future nursing payments paid by private insurance. This increased the share of nursing home expenditures paid by private insurance from 1 percent to 3 percent. Data on length of stay and spend-down trends under Medicaid were derived from a recent Brookings Institution study by the American Association of Retired Persons.<sup>27</sup>

## Notes

1. Including the effects of inflation, the cost of an annual stay in a nursing home will be \$190,000 in 2030.
2. This is for two visits per day by a home care aide costing \$54 per visit in 1997. National Association for Home Care (1997). *Basic Statistics About Home Care 1997*. Washington, D.C.: National Association for Home Care.
3. Coopers and Lybrand (1996). *An Overview of the Assisted Living Industry, 1996*. Fairfax, Va.: Assisted Living Federation of America.
4. American Health Care Association (1998). *Today's Nursing Facilities and the People They Serve*. Washington, D.C.: American Health Care Association.
5. Hobbs, F.B. and B.L. Damon (1996). 65+ in the United States *Current Population Reports* 23–190. Washington, D.C.: Bureau of the Census.
6. Ibid.
7. Bectel, R.W., and N.G. Tucker (1998). *Across the States 1998*. Washington, D.C.: American Association of Retired Persons.
8. See note 3 above.
9. Weiner, J., L.H. Illston, and R.J. Hanley (1994). *Sharing the Burden: Strategies for Public and Private Long Term Care Insurance*. Washington, D.C.: Brookings Institution.
10. Kemper, P. (1988), The Evaluation of the National Long-Term Care Demonstration: Overview of Findings, *Health Services Research* 23 (1):161–74; Weissert, W.G., C.M. Cready, and J.E. Pawelak (1988). The Past and Future of Home and Community-Based Long-Term Care, *Milbank Quarterly* 66 (2): 309–83; Alecxih, L.M.B., S. Lutsky, J. Corea, and B. Coleman (1996), *Estimated Cost Savings from the Use of Home and Community Based Alternatives to Nursing Facility Care in Three States*, Washington, D.C.: American Association of Retired Persons.
11. See note 9 above.
12. Jackson, B. (1994). A New Research: Implications for Product Design and Pricing. Paper presented at the 12th Annual Long-Term Care Insurance Conference, Coronado, Calif.
13. National Alliance for Caregiving and American Association of Retired Persons (1997). *Family Caregiving in the U.S.: Findings From a National Survey*. Washington, D.C.: National Alliance for Caregiving and American Association of Retired Persons.
14. U.S. Department of Commerce (1997). *Statistical Abstract of the United States 1997*. Washington, D.C.: Bureau of the Census.

15. MetLife Mature Market Group (1997). *MetLife Study of Employer Costs for Working Caregivers*. Westport, Conn.: MetLife.
16. Bachu, A. (1997). Fertility of American Women: June 1995. *Current Population Reports*. 20-449. Washington, D.C.: Bureau of the Census.
17. Affordability is defined as spending no more than 2 percent of income for ages 35-44, 3 percent for ages 45-54, 4 percent for ages 55-59, and 5 percent for ages 60-64 and ages 65+.
18. Coronel, S., and M. Kitchman, (1997). *Long-Term Care Insurance in 1995*. Washington, D.C.: Health Insurance Association of America.
19. American Health Care Association (1997). *Facts and Trends: The Nursing Facility Sourcebook, 1997*. Washington, D.C.: American Health Care Association.
20. Lewin-VHI, Inc. (1994). *Aging Baby Boomers: How Secure Is Their Economic Future?* Report prepared for the American Association of Retired Persons.
21. Mathew Greenwald & Associates (1997). *1997 Long-Term Care Survey—Report of Findings*. Washington, D.C.: National Council of the Aging and John Hancock.
22. See note 6 above.
23. Murtaugh, C.M., P. Kemper, and B.C. Spillman (1990). The Risk of Nursing Home Use in Later Life. *Medical Care* 28(10): 952-62.
24. U.S. Department of Commerce (1997). *Statistical Abstract of the United States 1997*. Washington, D.C.: Bureau of the Census.
25. Lifeplans, Inc. (1995). *Who Buys Long-Term Care Insurance?* Washington, D.C.: Health Insurance Association of America.
26. See note 16 above.
27. Wiener, J.M., C.M. Sullivan, and J. Skaggs (1996). *Spending Down to Medicaid: New Data on the Role of Medicaid in Paying for Nursing Home Care*. Washington, D.C.: American Association of Retired Persons.

## Authors

Janemarie Mulvey, Ph.D., is Director of Economic Research at the American Council of Life Insurance (ACLI). Her expertise includes cost forecasting, Social Security and pension issues. Prior to joining ACLI, she was an economist at the Urban Institute. There she co-authored a book with Marilyn Moon titled *Entitlements and the Elderly: Protecting Promises and Recognizing Realities*. Prior to the Urban Institute, Dr. Mulvey was a Senior Analyst in the Public Policy Institute of the American Association of Retired Persons (AARP). There, her research included elderly tax burdens, out-of-pocket health care costs, and the macroeconomic impacts of health care reform. She has a Ph.D. in Economics from George Mason University in Fairfax, Virginia.

Barbara R. Stucki, Ph.D., is a Senior Policy Analyst at the American Council of Life Insurance, where she focuses on long-term care and disability issues. Prior to joining ACLI, Dr. Stucki was a policy analyst for the American Association of Retired Persons, where she worked on long-term care issues including private-sector financing options, aging with a disability, and informal caregiving. Dr. Stucki also has conducted field research on the impact of urbanization on rural elders in West Africa. She has a Ph.D. in Anthropology, with emphasis on Gerontology, from Northwestern University in Chicago.



**American Council of Life Insurance®**

1001 Pennsylvania Avenue, N.W.  
Suite 500 South  
Washington, D.C. 20004-2599  
7358001