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Comparing discounted chronic illness riders with LTC riders

Sales Idea

The small print could cost more than you think

All long-term care (LTC) and chronic illness riders on life insurance pay benefits to individuals as a tax-free acceleration of the death benefit — but that's where the similarities end. You need to look at the small print to know what you have.

There is a misconception that certain chronic illness riders are "free". But "no charge" does not mean free. There is a back-end charge when the chronic illness rider is used — and that charge is taken from the chronic illness benefits your client may be counting on to help pay expenses. While these riders do not require specific underwriting and are not charged for up front, it is important to explain to clients that the charge to use the rider will come from the benefits they are accelerating.

How a "no charge" chronic illness benefit is calculated

These riders pay tax-free benefits through **IRC §101(g)** using the "Discount Method"; which is a back-end charge determined at claim time by an actuarial calculation. The discounting formula for a chronic illness benefit is based on several factors at time of claim including age, gender, and premium class, as well as discount interest rates and policy cash values. When a claim is filed and approved, the amount allowed for acceleration (usually up to 24% a year) is reduced by the calculated discount amount. For your client, that means that the amount of chronic illness benefits actually paid to the policy owner is less than the amount they accelerated. Funds from the acceleration that are not paid as chronic illness benefits are forfeited to account for the rider charge.

Because the chronic illness benefit is calculated at the time of claim, the amount you see on an illustration is not necessarily the chronic illness benefit amount that will be paid. In addition, the younger an individual is when filing a chronic illness claim, the more the benefit is discounted — resulting in more death benefit acceleration being permanently forfeited to pay for the rider. And women have a larger discount factor than men; with all other factors equal, women receive less than men in chronic illness benefits — and forfeit more!

Discounted chronic illness riders — IRC §101(g)
The following chart shows how discounting would affect a chronic illness rider benefit with no up-front charge on an Indexed Universal Life policy based on a female, age 50, and rated non-tobacco preferred. Premiums are paid to age 120 and 6% crediting rate used. Results will vary based on cash value and discount interest rates used at time of a claim.

Age at Election of Rider	Death Benefit Accelerated	Chronic Illness Benefit Paid	Amt. of Chronic Illness Benefit Forfeited
65	$300,000	$206,105	$93,895
70	$300,000	$218,064	$81,936
75	$300,000	$228,428	$71,572
80	$300,000	$238,058	$61,942
85	$300,000	$246,711	$53,289

Other things you should know about discounted chronic illness riders
Chronic illness rider and the base policy could be subject to the following:

- A permanent condition is usually required
- Premiums due must still be paid while on claim
- The policy may have an exclusion period (typically two years) before a chronic illness claim can be filed
- Chronic illness benefits are paid tax-free, but will be limited to the HIPAA per diem in the year of claim ($131,400 in 2018)[1]
- The insurance company may reserve the right to limit payment of chronic illness benefits on an inforce policy to a maximum amount (such as $500,000) even if the death benefit is higher

Long-term care riders offer more comprehensive coverage

- LTC riders offer tax-free benefits[1] though **IRC §7702B** — and what you see is what you get[2]
- The rider is medically underwritten up front, and monthly charges are paid, so the policy owner knows that their LTC benefit will be the full amount specified at issue[2] no matter when they need their LTC benefits
- The rider will pay for temporary as well as permanent claims as long as all claim requirements are met

LTC riders — IRC §7702B LTC riders

Age at Election of Rider	Death Benefit Accelerated	Long-term Care Benefit Paid	Amt. of LTC Benefit Forfeited
65	$300,000	$300,000	$0
70	$300,000	$300,000	$0
75	$300,000	$300,000	$0
80	$300,000	$300,000	$0
85	$300,000	$300,000	$0

Nationwide offers an LTC rider that

- Tells your client at policy issue what the LTC benefit will be[2]
- Accelerates 100% of the death benefit[2] regardless of when a claim begins
- Pays tax-free CASH INDEMNITY benefits — Nationwide places no restrictions on how benefits can be used, including allowing benefits to be used to pay for family care[1]
- Offers lapse protection while on LTC claim
- Receives status from **IRC §7702B**, which means important consumer protections are included

Know the difference BEFORE your client buys coverage

When your clients are covered with an actual LTC rider, they are assured of what their benefit will be[2] and can make long-term care plans with a defined LTC benefit amount in mind. LTC benefits with no surprises will; help make the converation with your client less difficult at claim time.

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[1] The amount a policy owner may receive tax free is the greater of the HIPAA per diem in the year of claim, or actual costs incurred. Please consult a tax advisor when paying family or informal caregivers as there may be tax implications.

[2] Assuming no withdrawals or loans

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