Washington State's New LTC Program: A Sign of Things To Come?

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Employees in Washington state are just months away from a new 0.58% payroll tax on their earnings, with no cap. With its Long-Term Care Trust Act, creating the WA Cares Fund, Washington has approved the nation's first state-sponsored long-term care (LTC) insurance program. Will other states follow and implement their own LTC insurance programs? It's too soon to tell. As a baseline, here's how Washington's plan will work:

Beginning with payroll earnings on or after January 1, 2022, most Washington employees will be subject to the new tax. There are some exceptions, including:

1. Workers under the age of 18
2. Employees of the federal government
3. Employees of federally recognized tribes, although they may opt into the program
4. Employees under a collective bargaining unit in existence as of October 19, 2017
5. Self-employed individuals, who may also opt-in

Moreover, certain employees who have qualifying LTC insurance contracts in effect prior to November 1, 2021, won't owe this tax, which amounts to $58 a year on every $10,000 of gross earnings. (This tax is paid only by the employee, not the employer.)

Note that employees in Washington with a qualifying LTC contract in place must attest to that fact and apply for the exemption to the new payroll tax. The Washington employment security department is not required to verify such coverage.[1]

Applications for exemptions will be accepted from October 1, 2021, to December 31, 2022. Once an exemption is granted, an exempt individual is permanently ineligible for the state-run plan. Individuals receiving an exemption will not be entitled to any refund of the 0.58% tax already paid under the WA Cares trust program.

Who Can Receive WA Cares Benefits?

The 0.58% WA Cares tax will begin collection in January 2022, with the first payouts coming three years later, in January 2025.

To be eligible for WA Cares payments, a beneficiary must have paid the 0.58% tax (officially known as long-term services and support premium) for the equivalent of either:

1. A total of 10 years, including 5 or more consecutive years without interruption; or
2. 3 years within the last 6 years.

An eligible beneficiary also must have worked at least 500 hours per year in either of those periods.

Eligible WA Cares beneficiaries must have paid the 0.58% payroll tax on their own earnings for the required periods. Spouses or dependents of participating employees won't qualify for WA Cares LTC reimbursements.

As for benefits, eligible services include assisted living, nursing homes, or adult daycare. Amounts paid by WA Cares to qualified individuals would be "benefit units" of up to $100 per day (inflation-adjusted), with a maximum of 365-lifetime benefit units. Thus, up to $36,500 could be paid to program participants to cover eligible LTC expenses.

Recipients must be residents of Washington state at the time of the claim, at least age 18, and they must meet the minimum level of required assistance with activities of daily living. Once a recipient has exhausted the lifetime benefit units ($36,500 in payments), WA Cares won't pay any more.

Any payments to an eligible beneficiary will not be counted as income or assets for other Washington state means-tested programs, such as Medicaid.

What Is a Qualified LTC Insurance Contract For WA Cares?

As mentioned, employees who are covered by a qualified LTC contract won't owe the 0.58% payroll tax.

According to Washington state law, LTC insurance is "an insurance policy, contract, or rider that provides coverage for at least 12 consecutive months to an insured person if they experience a debilitating prolonged illness or disability."

In addition to standalone LTC policies, Washington's Office of the Insurance Commissioner considers long-term care riders to life insurance policies and annuity contracts as a form of LTC insurance if they meet clearly defined benefit requirements.

For more information and a list of companies approved to sell LTC insurance in Washington state, visit: https://www.insurance.wa.gov/what-qualifies-long-term-care-insurance.

Considering WA Cares

The new WA CARES program appears to have some merits. A hypothetical Seattle-based employee earning $100,000 a year would pay an additional $580 a year in payroll tax, or $1,740 over the three years from 2022 until 2025.

If that individual needs LTC in 2025, WA Cares could pay for as much as $36,500 in LTC benefits. Even more, with an inflation adjustment. That would be a good return on $1,740 in taxes paid.

That said, few people are likely to go directly from a W-2 payroll to a need for LTC. An employee who is now age 55, for example, might retire at age 65 after paying into WA Cares for 10 years. If LTC is needed at age 80, no WA Cares benefit would be paid if that individual has since moved to another state.

An employee now age 56 might pay into WA Cares for 9 years until retiring at 65 and receive no payout at all, even in Washington state, if more than 6 years have passed.

In yet another scenario, an employee might meet all the requirements for WA Cares and still receive no payback if his or her spouse (not a WA Cares participant) is the one needing LTC.

Perhaps the most significant drawback of the WA Cares program is the relatively small size of the tax and the resulting maximum payment. The 2020 Genworth Cost of Care survey puts the average cost of a nursing home private room at $11,954 per month in Washington. Assisted living and at-home care average around $6,700 a month in Washington: nearly twice the maximum total payout from WA Cares.[2]

Indeed, the best feature of the WA Cares Fund might be the exemption offered to employees who already have or who soon acquire a qualified LTC contract. The new law highlights LTC costs, encouraging workers who might not need such care for many years to look into such coverage when they are relatively young and might find well-priced insurance.

LTC Expenses in Retirement

The above numbers for LTC costs in Washington state are by no means extraordinary. The national average cost for a semi-private room in a nursing home facility is $7,756 per month; for a private room, the number increases to $8,821 per month.[3] LTC costs have been rising and are likely to keep escalating as the Baby Boom generation goes through extended life expectancy.

In all 50 states, the rising cost of LTC is a growing threat to those approaching retirement, with little to no assets saved for these charges. The WA Cares

Fund is a noteworthy effort to meet the need for affordable LTC costs, but the $36,500 maximum benefit is a drop in the bucket compared to what many will likely pay out of pocket for such care.

What's more, Medicare doesn't cover most LTC costs, which many retirees fail to realize. Medicare only covers LTC or custodial care costs when medical care is involved. Help with activities of daily living such as bathing and dressing, which comprise most LTC, is generally not considered medical care.

Survey after survey shows that a leading concern among retirement-aged adults is the cost of health care, including LTC. 7 out of 10 people will require long-term care in their lifetime.

Nevertheless, nearly half of those surveyed have no plan to address the costs of a health event[4]. If you are not addressing these concerns with your clients, you are doing them a grave disservice.

Risk Reduction

One way to address LTC risk is to purchase a standalone LTC insurance policy. Acquiring a product from a reputable insurer will provide some relief if any LTC need stretches into multiple years and a huge financial drain.

LTC policies may not be an easy sell. Buyers face the prospect of spending substantial amounts of money on premiums for years and getting a scant return on those outlays if LTC claims turn out to be minor or nonexistent. That's especially true if clients are young and healthy, without a family history, including expensive LTC outlays.

Such objections might be addressed by comparing LTC insurance to home or auto insurance. Most people pay for such coverage year after year and seldom make a claim that results in a payment. Yet, these insurance premiums are not considered wasted, as the insured parties are grateful to avoid severe incidents with their homes or vehicles.

The same advice might be offered for LTC insurance. If you need to cover six-figure LTC costs, it's great to have insurance. Alternatively, if LTC need ends up being manageable, people may be glad for their good fortune.

Another approach is to suggest acquiring LTC coverage as an adjunct to a product with a specific return. For example, some permanent life insurance policies offer an LTC rider as an option. This coverage will come in handy if costly LTC should be needed, but there will likely be a sizable payment to a beneficiary if the policy is maintained until death.

An alternative for clients who are not inclined or unable to get life insurance is to buy an annuity with an LTC rider. Again, there will be some benefit—in the form of cash flow—if the LTC option is never exercised.

Tax-Efficient Planning

LTC risk reduction also may be obtained by establishing a Health Savings Account (HSA). People with certain high-deductible health insurance policies may have an HSA and make fully tax-deductible contributions each year, up to $9,200 in 2021 for families with both spouses 55 or older. High-deductible health insurance policies have lower premiums than policies with low deductibles, so the former can work well for healthy people who usually avoid costly medical bills.

Any investment gains inside an HSA also may be tax-free. HSA withdrawals are untaxed if the money is used for qualified expenses: expenses on the permitted list include premiums for standalone LTC insurance, up to age-based limits.

For example, people in the 61-70 age range can deduct LTC policy premiums up to $4,520 in 2021. Thus, a couple aged 55 or older with an HSA could put the maximum $9,200 into the account and use up to $9,040 to pay premiums on an LTC policy with dollars that were never subject to income tax.

If clients prefer buying life insurance with an LTC rider, the portion of the premium attributable to LTC coverage could be deductible. After paying for LTC insurance, any money left in the HSA could be invested for the long term, building a fund to help pay health care expenses over a long retirement.

Advisor Action Plan:

- Encourage clients covered under high-deductible health insurance to max fund their Health Savings Accounts. The contributions are tax-deductible, and withdrawals are tax-free if used for qualified medical expenses.
- Remind clients that contributions to HSAs are not permitted once they are enrolled in Medicare.
- Assess relevant factors for determining the type and amount of LTC coverage or assets earmarked for LTC, such as current age, gender, and health conditions.
- Evaluate the cost of LTC in each client's state of residence, which can vary significantly.
- Discuss the use of riders on annuity contracts and insurance policies that may be utilized in the event of a chronic illness or the need for LTC.

Sources:

[1]Substitute House Bill 1323 Sec.5 (3) – effective date July 25, 2021

[2]https://www.coldstream.com/blog/2021/04/26/new-washington-state-long-term-care-act/

[3]https://www.genworth.com/aging-and-you/finances/cost-of-care.html

[4]Healthview Services – The Long-Term Value of an HSA, May 2020.