

The coming wave:

Professional liability lawsuits for failure to recommend a realistic plan for long-term care

Synopsis:

No reasonable financial planner doubts that client's are expected to live a long life after retirement: portfolio payout calculations routinely take into consideration a life expectancy into the early 90's. Less often considered is the need for long-term care and the serious impact it has on the best thought out retirement plan. Failure to talk about these consequences may subject financial planners to a claim of breach of due diligence.

A real story

Sheila Adams (not her real name) is a seasoned financial planner with a major mid-west insurance company. She is also one 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. Apparently talking about it that may not be enough.

Ms. 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 lifesavings. 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.

Living a long life is a near certainty, planning for it a necessity

A July 14th, 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 70+ Americans have dropped between 5% and 20% in the past few years;
- By 2035 this group will more than double to 57 million;

- The fastest growing segment of the US population is 85 +;
- Insurers count family history far less if people reach 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 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. Rarely however do financial planners discuss with clients the impact providing care will have on their relationships with family members and family finances.

The need for long-term care must be discussed

Basic to the identity of financial planners is their reputation as professionals. A fundamental risk to their carefully crafted and protected image as a professional is talking about a subject they do not have mastery over. Although many will expose the risk, few will engage in a formal discussion of the impact long-term care has 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 not skilled care. Custodial care is defined as assistance with ones 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 that 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 matter 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 is a critical part of 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 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 VA 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 and or rehabilitative care. Although never intended to do so, the program routinely paid for custodial care prior to 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 and 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 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 site the Veterans Administration as a source of funding for custodial care. It is not. The VA may pay for care but in only limited situations and usually requires a financial contribution. In point of fact the federal government has stated as much by encouraging active and retired military personnel to purchase 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.

Many financial planners see long-term care insurance 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 than 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 CFP to CLU reinforces this basic principal of professional conduct by teaching how to ask the right questions and work with other professionals such as estate planning attorneys and CPA's to draft the right plan. Although financial planners are certainly subject to malpractice claims it is less likely that they 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. Doing so would lead to a discussion of the consequences of not having a plan rather than focusing on risk coverage.

In turn this leads to the establishment of a plan for providing care. All plans must be protected with insurance. It's just like selling life insurance. If the subject is

brought up it is usually in the context of suggesting LTCi as a way of protecting assets not protecting a plan for long-term care. This creates the 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:

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 that they can self-insure the cost;
6. Not reviewing existing policies carefully for proper application to the client;

“I talked with the prospect about LTCi and he didn’t purchase 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 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 through 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 (read: 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 its intent was not to absolve the producer of liability but rather as a sales gimmick to embarrass the person into purchasing the product.

“My client purchased 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 \$50.00 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. Worst, if the individual needs skilled nursing home care he 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.

Arguing, “some coverage is better than none” at best is amateurish and at worst exposes the financial planner's lack of understanding how long-term care impacts a family and its retirement plan.

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. He or she 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% (plus state income tax).

The family argues that the producer should have considered the tax consequences of cashing in qualified funds. Had he 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 or her responsibility to exercise due diligence in protecting the financial interests of his client.

“I read in *Consumer Reports* that *my* client doesn’t need LTCi if he has more than \$1,500,000.”

It’s puzzling when a seasoned financial planner tells a client he or she does not recommend LTCi to wealthy clients. The same professional will usually go out their way to recommend a Medicare supplement policy to the same person. 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.

“I work with an attorney who believes that for families with modest estates a LTCi 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 suggest 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, a federal and state program based on financial need 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 expires 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 he 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 cost-based assets. Gifting them also transfers that basis. Result: A 15% 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 facility. The only choice left is to make a placement thus having Medicaid pay or re-transfer the funds back.

There is little doubt that the attorney will 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 is a profession that requires the same commitment financial planners make to the financial and estate planning profession.

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 client's 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 assertively.

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 including that clients absolutely believe they will live a long life. They so much as tell financial planners that every time they ask for reassurance principal will remain intact after retirement. Establishing this base line leads to;
3. A discussion of the consequences long-term care has on a family and their 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 planner to talk about consequences needing care will have 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. That since 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 (LTCi) has been purposely left to 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 choice and not being a burden, not in the context of protecting a plan. The presentation is product not advice driven and then 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 LTCi, financial professionals are well advised to make the commitment to understand the profession of 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.

Harley Gordon is a founding member of the National Academy of Elder Law Attorneys, a trade group representing over 4,000 attorneys focused on elder law issues. He has created along with other industry experts, the "Certified in Long-Term Care" (CLTC) designation which currently has over 7,000 graduates. The program is committed to increasing the sale of long-term care insurance based on same sound financial and ethical precepts that guide the professions of financial and estate planning.