BROKER WORLD

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# Willy Wonka And The LTCI Factory

***"Come with me, and you'll be in a, World of pure imagination…"***

I recently attended an LTCI brokerage conference featuring the latest product designs from a variety of carriers. A walk through the aisles was much like a walk through Willy Wonka's Chocolate Factory where, despite general perception, there is more to a chocolate bar than just sugar and chocolate. Likewise there is more to LTCI policy designs than just a limited, cookie-cutter approach. You have options. Multitudes of them.

Granted, we all know that the number of companies offering stand-alone LTCI products has decreased significantly over the past decade. Yet as the remaining carriers have begun targeting different market segments, specialized product designs have become more common. Now the age of imaginative product designs has commenced–from traditional higher-end products aimed at affluent buyers, to more basic affordable products for the middle market. From programs catering to worksite sales with simplified underwriting, to others providing dividends or benefit credits that mimic dividends.

This year, for the first time in a decade, a new carrier has entered the LTCI marketplace offering a stand-alone product with lifetime benefits, 10-pay, single pay, return of premium available with and without a claim's offset, cash surrender options, and an emphasis on selling compound inflation protection. These benefits, all of which used to be routinely offered, have either disappeared or been deemphasized as the LTCI market contracted over the past decade. With all of the additional sales opportunities utilizing these features once again available, many agents are beginning to feel like a kid in a candy store.

*"We'll begin, with a spin…"*

**Sales Opportunities with Limited Pay and Richer LTC Benefits**

***The Reverse Combo.*** The emerging popularity of life combo products has actually opened up new, competitive possibilities for the stand-alone product. Taking the stand-alone LTCI base product and adding both a return of premium rider and a cash surrender option creates a product that mimics life combo products. Since the base policy is an LTCI policy with the life insurance benefits added on, I call this product, the "Reverse Combo".

Life insurance regulations require the life combo product to have cash values at certain minimum levels and death benefits at levels in excess of those cash values. This means that clients buying a life combo product primarily for the LTCI protection wind up paying for much more life insurance protection than they ideally want. These clients also may not get ideal LTCI coverage because life combo products often cannot offer the full range of inflation protection options or premium payment options that create more LTCI leverage. The reverse combo product, on the other hand, follows LTCI product regulations, which have no minimum cash values, death benefit, or premium payment requirements. Thus, the cash

| REVERSE COMBO<br>Joint Policy Age: 60, Single Premium: $100,000, COLA: 3%<br>Benefit Period – 3 Year / No Extension<br>LTC Daily Benefit – $135 per day per person | | | |
|---|---|---|---|
| Years After Issue | LTC Maximum Benefit | Cash Surrender Option | Death Benefit |
| 1 | $295,560 | $10,000 | $100,000 |
| 2 | 304,472 | 20,000 | 100,000 |
| 3 | 313,560 | 40,000 | 100,000 |
| 4 | 322,966 | 60,000 | 100,000 |
| 5 | 332,655 | 80,000 | 100,000 |
| 10 | 385,639 | 80,000 | 100,000 |
| 15 | 447,061 | 80,000 | 100,000 |
| 20 | 518,266 | 80,000 | 100,000 |
| 25 | 600,813 | 80,000 | 100,000 |
| 30 | 696,507 | 80,000 | 100,000 |

surrender option can be graded up over a period of years and the return of premium can be designed as a second-to-die benefit, freeing up significant cost savings to fund increased LTCI coverage. Also, the more flexible reverse combo regulations allow both death benefits and LTCI claims to be paid out, so clients need not spend their own life insurance benefits first to pay for long term care costs. The reverse combo can be purchased in any combination of inflation options, benefit periods, and premium payment options, with or without the cash surrender values in order to customize LTCI coverage more precisely to the client's needs.

*"What we'll see, Will defy explanation…"*

***Executive Carve-Outs.*** For the past several years 10-pay premium options and lifetime benefit periods have been unavailable on LTCI products. This had minimized the use of a popular tax advantaged sale—offering key executives employer paid and fully deductible LTCI benefits without any tax ramifications to the recipient. However, with 10 pay and lifetime benefits available once again, this tax incentive may become popular with those agents operating in the advanced underwriting, upper income markets. Here's the basic premise: Corporations can create a substantial executive benefit using pre-tax dollars by deducting the cost of the 10-pay LTCI premiums as a normal and ordinary business expense, so that the benefit is fully paid up for the key executives during their working lifetimes. Perhaps the most amazing aspect of this sales opportunity is that the business expense deducted by the company is not viewed by the IRS as imputed income for the key executive, nor is it subject to any employer discrimination testing, and all of the reimbursed LTCI costs are tax-free when paid to the insured. Also, the policies are fully paid up after the tenth year and no longer at risk for future rate increases since no future premiums are ever due.

***Advanced Executive Carve Outs Using Full Return of Premium.*** There are other possible creative variations on the executive carve out concept. Here is one idea to test with your accountant. Full return of premium does not require the client to use the death benefit before LTCI claims are paid. Therefore, a solution similar to COLI is available. The corporation purchases a 10-pay with the full return of premium and assigns the ROP benefit to the corporation. The corporation is guaranteed to receive all premium payments back and thus may be able to hold the full amount of those premium payments as a corporate asset on the balance sheet in addition to the cash asset generated by the actual tax savings received from deducting the 10-pay premiums.

*"If you want to view paradise, Simply look around and view it…"*

***1035 Exchanges.*** The Pension Protection Act, passed in 2006 with a delayed effective date until 2010, allows another significantly tax-advantaged sales opportunity for stand-alone LTCI policies. For individuals who own a non-qualified annuity, they can take the principal and deferred tax buildup of the annuity and execute a 1035 tax-free exchange to pay the premiums for the stand-alone LTCI policy. Since the stand-alone benefits are received tax-free, the deferred interest on the annuity is never subject to future taxation. While this benefit has been available in the stand-alone market since 2010, tracking and administering the annual cost basis associated with paying premiums each year is onerous for both the company and the insured. However, by using a single pay stand-alone LTCI policy, the deferred tax buildup is immediately eliminated and there are no remaining cost basis issues. There are also advanced possibilities using this concept in combination with the return of premium, but, as always, please consult your tax advisor.

*"Wanna change the world? There's nothing to it…"*

There are in fact many different LTCI solutions available to serve the 78 million baby boomers approaching retirement–a group which represents about a quarter of the U.S. population. Many of these boomers are currently dealing with the burden of having to pay for long term health care costs for one of their relatives. The majority of this fast growing demographic does not realize that looming long term care costs can be solved with an array of insurance solutions already available in the market. I expect to see continued innovation addressing many of these market segments with carriers gravitating toward the solutions that prove most popular. The government also has been receptive over the past few years to support private alternatives and increase existing tax incentives, as the majority of the long term care burden eventually falls on state and federal budgets through Medicaid. Luckily, this looming crisis can still be prevented from becoming a catastrophe. The cost of insuring against this future risk is accessible to many Americans as long as they plan in advance, while still young and healthy enough to obtain coverage.