

1035 REASONS YOUR ANNUITY CLIENTS WILL TALK TO YOU ABOUT LTC

By JESSE SLOME

Americans love their annuities, as well they should. Over the past five years, they have invested almost \$1 trillion in this favorite retirement planning vehicle. Chances are, you may have sold one or two fixed or variable annuities ... maybe you've sold quite a few more.

In fact, 2001 was the last year annual U.S. annuity sales were below \$200 billion. And, annuity owners like dealing with insurance agents and brokers because they account for roughly 60 percent of all U.S. annuity sales.

What we also know to be true is that far too few individuals have undertaken any planning for long-term care (LTC). Their reasons are plentiful and honestly, hard to overcome. It's even harder to convince an individual who has diligently set aside retirement funds which, in their minds, can be utilized should a need for care arise. I have 'what if' savings so why buy something I might never need or use is the common objection.

But a new opportunity awaits agents and as interest rates rise, the opportunity can be expected to grow exponentially. The opportunity targets millions of aging individuals who have their 'what if' money already invested in an annuity. An increasing number of agents are successfully utilizing Section 1035 exchanges to help clients repurpose existing annuities into a linked-benefit annuity that provides both continued tax-deferred growth along with significant tax advantages and leverage should a need for long-term care arise.

"Americans have nearly \$3 trillion in fixed and variable annuities set aside as part of their retirement planning strategy," reports Chris Coudret, vice president and chief distribution officer at OneAmerica. "Many of these individuals could benefit by taking advantage of a 1035 exchange, which could



offer tax benefits as well as provide long-term care benefits, should they be needed."

What are 1035 exchanges and more importantly how can you effectively communicate their benefit to your annuity clients? Let's explore this opportunity.

1035 EXCHANGES: A POWERFUL TOOL

The Section 1035 Exchange provides a powerful tax-advantaged way to repurpose an existing annuity or life insurance policy to one that also provides long-term care benefits.

Part of the Pension Protection Act (PPA) passed by Congress in 2006, the 1035 provision became law in 2010. Arriving on the heels of the Great Recession, it's no wonder that little attention was paid:

But that has changed. Many Americans, including those already retired, are again feeling more financially secure. Millions of these Medicare beneficiaries realize they are now closer to the age when LTC services may be needed.

A key benefit of the PPA allows withdrawal of funds from a qualifying annuity to pay LTC costs income tax free. Monies withdrawn from annuities that do not meet PPA provisions may be subject to taxation—even if

USING YOUR TRADITIONAL ANNUITY

TO PAY FOR LTC EXPENSES

\$200,000 currently available in a non-qualified annuity
Annuity owner, age 66 and spouse, age 62

BEFORE

\$5,000

Partially Taxable

Withdrawals of \$5,000/Month to pay for LTC

Roughly 40 months of withdrawals
Withdrawals are taxable to extent of gain

USING A 1035 EXCHANGE TO REPURPOSE INTO A PPA-QUALIFIED LINKED-BENEFIT ANNUITY

AFTER 1035

\$5,000

Income Tax-Free

\$200,000 exchanged to a linked-benefit annuity
Spouses, ages 66 and 62

Withdrawals of \$5,000/Month to pay for LTC

Lifetime (unlimited) – payments, income tax-free

they are used to pay for LTC expenses. The example shown depicts how a single annuity presently valued at \$200,000 can be repurposed into an annuity that provides a lifetime of LTC \$5,000 monthly payments for both spouses. The benefits are received income tax free and if neither spouse needs LTC and the second spouse dies at 94, the linked benefit annuity pays the designated beneficiaries \$202,000.

IDEAL 1035 EXCHANGE ANNUITY PROSPECTS

The ideal annuity owner to explore a 1035 exchange for an Annuity + LTC PPA compliant annuity generally will have owned their annuity for a sufficient period of time that any surrender charges have ended or are minimal. While some experts argue that the value of added leveraged LTC benefits and the potential tax advantages can be worth a nominal surrender charge, my contention is that an annuity free of charge is your ideal candidate. That

said, as interest rates start to climb, a higher new money rate could compensate for charges,

"Annuity owners in their 60s and-70s are ideal," explains Craig Matesky, president of ACACIA Insurance Services, headquartered in Newport Beach, CA. "They are not comfortable self-funding their LTC risk and are turned off by the 'use it or lose it' nature of traditional health-based LTC insurance."

What they find attractive is the added leverage along with the tax advantages, Matesky points out. A 70-year-old with an annuity currently valued at \$125,000 could withdraw \$5,500 a month to pay for LTC. But, some of the payments could be subject to taxation and after 23 months the annuity would be depleted.

By repurposing the current annuity into a linked-benefit Annuity + LTC policy, they gain the increased leverage of \$503,000 of tax-free LTC benefits. At age 85, the LTC pool is \$543,000 with monthly benefits of \$5,600 for up to 72 months.

STRATEGIES FOR APPROACHING CLIENTS

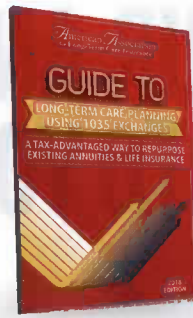
Imagine a long-term care insurance marketing strategy where you don't have to scare prospects? Even better, envision offering them a solution with no out-of-pocket expenditure.

That is the significant appeal of marketing 1035 exchanges to your existing annuity clients. You can simply explain that changes in the tax law have been implemented because Congress understood that Americans like annuities as a way to set aside funds for retirement and recognized adding tax advantages would motivate more people to avoid dependence on Medicare and Medicaid (Medi Cal) for their long-term care.

New AALTCI Online Guide Explores 1035 Exchange

A 24-page guide focused on 1035 Exchanges has just been created by the American Association for Long-Term Care Insurance.

To access or download the guide go to www.aaltci.org/1035



Their current annuity is an ideal retirement savings vehicle. But, Congress and the IRS approved features and benefits that offer improved options. And, just as people trade in their cell phones for new versions that offer greater options and benefits, it can be worth considering new versions of these annuities.

The "No-Cost Long-Term Care Plan" offering the potential of unlimited, 100 percent tax-free payments should you (or your spouse) need long-term care should be a sufficiently enticing offer to generate interest.

Finally as interest rates rise, annuity products offering LTC linked benefits should continue to be more attractive. That will encourage more companies to enter the marketplace.

According to LIMRA even as the number of companies offering Annuity + LTC combination products declined from eight companies in 2011 to five companies in 2016, sales have increased 23 percent on average annually since 2011. While the amount is miniscule in terms of overall new annuity sales (\$480 million in 2016), we are undertaking an aggressive consumer awareness campaign. If past efforts are a predictor of future results, I have never been more optimistic.

Often the one who enjoys the greatest success is the first to jump on-board. In my humble opinion, after three decades focused on long-term care insurance planning, this is the time to jump on this opportunity. ★



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