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LTCI + SPIA = A Dynamic Combination

How are long term care insurance (LTCI) policies and annuities alike? Both vehicles provide benefits to those who live long lives. A long term care insurance policy provides coverage for the costs of care needed over an extended period of time. An annuity produces an income stream that cannot be outlived. Imagine what these two important products can do when they work in tandem.

Here's an idea. A client may use an unproductive asset that is not needed, to purchase a single premium immediate annuity (SPIA). The income stream generated by the SPIA can, in turn, be used to help pay premiums on a long term care insurance policy.

Some of the income produced by the SPIA will be subject to income tax and some will not. The amount of income not subject to income tax is determined by the exclusion ratio.¹ The exclusion ratio solves for a percentage of the income stream that is deemed to be a return of basis and not included in taxable income. The balance of the income received is taxable income. When the basis has been fully recovered, all of the income will be subject to income tax.²

Premiums paid for HIPAA-qualified long term care insurance may be eligible for an income tax deduction. To the extent that medical expenses incurred for the tax year, including the lesser of the LTCI premium or the government provided age-based maximum amounts, exceed 7½% of the client's AGI it can be taken as a deduction.³



General Electric Capital Assurance Company, First Colony Life Insurance Company and GE Life and Annuity Assurance Company are members of the Insurance Marketplace Standards Association (IMSA). Membership promotes ethical market conduct for individual life insurance and annuity companies.

¹ IRC §72(b). The calculation is based on the age, life expectancy, and income option selected.

² Applies to those annuities with a start date after December 31, 1986.

³ IRC §213 (a) and (d).

Genworth Financial companies include:

First Colony Life Insurance Company, Lynchburg, VA
GE Life and Annuity Assurance Company, Richmond, VA
General Electric Capital Assurance Company, Lynchburg, VA
Capital Brokerage Corporation, Stamford, CT

Variable products issued by GE Life and Annuity Assurance Company
Principal underwriter: Capital Brokerage Corporation (dba GE Capital Brokerage Corporation in MN, IN, NM and TX),
3001 Summer Street, P.O. Box 120041, Stamford, CT 06912-0041 Member NASD/SIPC

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If the SPIA income stream is directly deposited into a client's checking account and the long term care insurance policy is paid by draft against this same checking account, it becomes an easy transaction for the client.

Further, if the client ever needs long term care, the benefits from the qualified long term care insurance policy are paid income tax free. LTCI premiums stop at that time, but SPIA income continues for the client's life, thereby helping to supplement income for long term care needs.

AN EXAMPLE:

The client is a male age 60. He wants to purchase qualified long term care insurance and would like to fund it with a single amount. He has \$100,000 in an account that he does not need.

He can use this asset to purchase a SPIA. The annual income based on a life-only income option would be \$7,352.78, based on current rates. Of this amount, \$4,051.38 would be a non-taxable return of premium and \$3,301.40 would be included in taxable income each year for the next 24 years plus part of year 25. At this point his basis would be fully recovered and 100% of the income received would be taxable as income. The additional income tax generated by the SPIA income stream, assuming a 35% income tax rate would be \$1,155.49. If the client lives past life expectancy, he will pay tax on the entire SPIA income. If he is still in the 35% tax bracket, income tax would rise to \$2,573.47.

The long term care insurance premium was calculated to be \$5,011.20 annually. Since he personally purchased the long term care insurance policy the client would be able to include the lesser of the premium (\$5,011.20) or the age-based eligible amount (\$980) with his other medical expenses incurred during the tax year and take an income tax deduction of the amount by which such expenses exceed of 7.5% of his adjusted gross income.

TO SUMMARIZE:

\$7,352.78	Annual SPIA income
5,011.20	minus long term care insurance premium (Unlike life insurance premiums, long term care insurance premiums are not guaranteed.)
<u>1,155.49</u>	minus additional income tax on SPIA income
1,186.09	Excess annual SPIA disposable income. If the client outlives his life expectancy, however, additional tax on SPIA income could rise to \$2,573.47, leaving a shortfall of \$231.89.

This example is for illustrative purposes only.

WHAT HAS BEEN ACCOMPLISHED BY USING THIS TECHNIQUE?

Long term care expenses will be available, if needed, from the long term care insurance policy.

The balance of the client's estate can remain intact to pass to the client's heirs. If long term care expenses are needed at some point in the future, they can be met by the long term care insurance policy. Estate assets will not have to be liquidated to meet these expenses. The estate can pass on to the client's heirs as he/she wishes.

An unneeded asset has been made productive. An asset such as a CD or a money market account may be part of a client's lifetime accumulation. Adequate resources for retirement may have grown over the years so that this may be an asset identified as no longer being necessary to fund retirement income, education costs or emergency needs. It may instead be available to purchase a SPIA to provide the income stream used to fund the long term care insurance policy.

An asset may be removed from the client's estate, thereby reducing the size of the estate and the potential estate taxes. An unneeded asset has been used to purchase a SPIA. If the income option is life only, the SPIA will have no value upon the client's death and will, therefore, not be included in the estate. One note of caution is that the SPIA terminates (with no additional income being paid) upon the death of the client, whenever that may be; even if death occurs after receiving only one payment from the SPIA. Clients may want to consider a SPIA offering a period certain.

The discussion of tax treatment in this material is Genworth Financial's interpretation of the current tax law and is not intended as tax advice. The clients should consult a tax professional for information related to their particular situation.