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CareMatters II
A quick look at tax incentives for businesses

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The ACG

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When evaluating the purchase of a variable annuity, your clients should be aware that variable annuities are long-term investment vehicles designed for retirement purposes and will fluctuate in value; annuities have limitations; and investing involves market risk, including possible loss of principal.

This information assumes that the life insurance is not a modified endowment contract, or MEC. As long as the contract meets the non-MEC definitions of IRC Section 7702A, most distributions are taxed on a first-in/first-out basis. Surrender charges may apply to partial surrenders. Loans and partial surrenders from a MEC will generally be taxable, and if taken prior to age 59 ½, may be subject to a 10% tax penalty. Loans and partial surrenders will reduce the cash value and the death benefits payable to your beneficiaries, and withdrawals above the available free amount will incur surrender charges. If your contract were to lapse with a loan outstanding, the loan amount in excess of basis will be treated as a distribution and all or a portion will be subject to income tax.

The underlying investment options to a variable annuity or life insurance product are not publicly traded mutual funds and are not available directly for purchase by the general public. They are only available through variable annuity/variable life insurance policies issued by life insurance companies.

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As your clients' personal situations change (i.e., marriage, birth of a child or job promotion), so will their life insurance needs. Care should be taken to ensure these strategies and products are suitable for long-term life insurance needs. You should weigh your clients' objectives, time horizon and risk tolerance as well as any associated costs before investing. Also, be aware that market volatility can lead to the possibility of the need for additional premium in the policy. Variable life insurance has fees and charges associated with it that include costs of insurance that vary with such characteristics of the insured as gender, health and age, underlying fund charges and expenses, and additional charges for riders that customize a policy to fit your clients' individual needs.

Not all Nationwide products and services are suitable for all clients or situations. There may be products, issued by other companies, which better suit your clients' goals. Be sure to consider your clients' objectives, their need for cash flow and liquidity, and overall risk tolerance when using any strategy.

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Agenda

- Structure of CareMatters II
- Hierarchy of CareMatters II tax advantages
- Value of the “above the line” deduction
- Corporate and business tax advantages
- Designing a CareMatters II policy for maximum tax advantages

CareMatters II structure is key……

Qualified LTC Contract per IRC § 7702B

Separately identifiable premiums

Fixed Premium Universal Life Insurance (holds all cash value) → "Life insurance" premiums not deductible

LTC Rider → Tax deductible

Extension of Benefits rider → Tax deductible

Inflation Rider → Tax deductible

LTC Premiums (have no cash value)

CareMatters II is the only Nationwide LTC product with separately identifiable premiums

The Value of an “Above the Line” Deduction

Gross Income

minus ----------- *Above the line deductions (expenses to a business, etc.)*

establishes **Adjusted Gross Income (AGI)**

Adjusted Gross Income (AGI)

Minus --------- *Standard & Itemized Deductions (below the line deductions)*

establishes **Taxable Income**

- An “above the line” income tax deduction can be taken whether you itemize deductions or not – thus may be more valuable
  - LTC deductions taken “above the line” are not subject to the 7 ½ % floor (but may be subject to age-based limits)
- “Below the line” deductions require that you itemize - and some deductions have a floor percentage that must first be reached before the deduction can be taken

CareMatters II - Hierarchy of Tax Advantages

The value of tax advantages varies by business entity and individual opportunities

Most valuable	More valuable	Valuable	Valuable
Business purchases for C-Corp owner/EE – or - Any business entity purchases for an employee	**Pass Through Entities – Self-employment health insurance deduction**	**Individual tax deduction**	**Use HSA distributions to pay LTC premiums**
LTC Premium 100% tax deductible as a business expense	LTC Premium tax deductible up to age-based limits taken "above the line"	LTC Premium tax deductible up to age-based limits - subject to 7 ½ % floor	May pay LTC Premium – up to age-based limits with HSA distributions

CareMatters II is the only Nationwide LTC product eligible for these tax advantages

CareMatters II - **Employee** LTC benefits for

C-Corp owner/EE, Non-owner/EEs & Less than 2% owner/EE of an S-Corporation

Business

sends premium

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Issues policy to

- **C-Corp Owner/EE,**
- **Non- Owner EE, or**
- **< 2% Owner of S-Corp**

- **Life insurance premiums** are treated as a compensation bonus
  - 100% tax deductible to business as a business expense (paid compensation)
  - 100% taxable to employee as compensation received
- **LTC premium** treated as payments for an accident & health plan
  - LTC premiums 100% tax deductible to business (no age-based limits)
  - LTC premiums are totally excluded from employee's income (no taxation)
  - LTC benefits paid tax free per IRS guidelines
- May include spouse and dependents
- Employer may not have any ownership or beneficial rights

LTC insurance may not be offered as part of a cafeteria plan under IRC § 125(f),

CareMatters II - Pass-through entities

LTC coverage for self-employed business owners

- Self-employed individuals may deduct qualified LTC premiums
  - Above the line deduction (not subject to 7 ½ % floor)
  - May include spouse and dependents
    - Cannot deduct LTC premiums in any month in which either spouse is eligible for subsidized LTC benefits from another employer
  - Deduction is subject to age-based limits

Attained age before end of tax year	2018	2019	2020
40 or under	$420	$420	$430
41-50	$780	$790	$810
51-60	$1,560	$1,580	$1,630
61-70	$4,160	$4,220	$4,350
71+	$5,200	$5,270	$5,430

- Each entity has slight variations in how premiums are paid and labeled for:
  - more than 2% owner of an S-Corporation
  - Partnership or LLC (paying taxes as a partnership)
  - Sole Proprietor

Please consult a tax advisor for details on how each business entity reports and deducts LTC premiums

Advantage of buying **CareMatters II** through the business

Advantages:

- For C-Corp owner
  - Tax efficient use of retained earnings to buy LTC coverage for owner/employee and select non-owner employees
- For pass through entity business owners
  - Not subject to 7 ½ % floor to get income tax deduction for LTC premium

Considerations:

- C-corp. owner and employee can utilize shorter premium schedules
  - Shorter premium schedules purchase more LTC coverage
    - with no waste of tax deduction since 100% of LTC premium is deductible
  - Life insurance premium should be “reasonable and necessary”
- Pass-throughs may want to consider whether:
  - longer premium schedules are worth capturing more tax deductions
  - vs. buying a larger LTC benefit with a short premium schedule but losing some tax deductions to age-based limits

Maximum deductions are in the Inflation

C-Corporation Owner/Employee –

55-year-old male, non-tobacco, couples rate paying $20,000 premium for 5 years with a 6-year LTC benefit

	No Inflation	3% Compound Inflation
$20,000 Premium paid over 5 years	$20,000 X 5 = $100,000 total	20,000 X 5 = $100,000 total
Death Benefit	$182,564	$130,884
Total LTC benefits policy year 1	$547,963 - $7,607 per mo.	$423,307 - $5,454 per mo.
Total LTC benefits at age 80	$547,963 - $7,607 per mo.	$886,311 - $11,418 per mo.
Life insurance premium	**$16,092**	**$11,536**
LTC Rider premium	$1,383	$992
Extension of Benefits rider	$2,525	$1,810
Inflation rider	N/A	$5,662
Break even age on inflation		Age 67
Annual total deduction to the business[1]	**$20,000 (total $100,000)**	**$20,000 (total $100,000)**
Total annual amount paid that is included in owner/employee's income	**$16,092**	**$11,536**
Annual for LTC premiums paid by business - but excluded from employee's income	**$3,908**	**$8,464**

Adding inflation reverses premium exposure from life to LTC

– Reducing life insurance premium reduces taxable compensation

- Make sure to consider "break even" age for older applicants

In Summary

- Business owners can maximize tax advantages by purchasing CareMatters II through the business
    - Tax deductions help make the policy more affordable and more desirable of a purchase

- Business owners are afforded more liberal LTC tax advantages than individual taxpayers
    - C-Corporations get 100% deduction of LTC premiums
    - Owners of pass through entities avoid the 7 ½ % floor requirement - ensuring they get their LTC tax deduction (subject to age-based limits)

- ***CareMatters II*** offers **cash indemnity** LTC benefits that will help the policy owner to maintain choice, control and flexibility.

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