



A Primer on Life Insurance and Planning in a Global Market

By Leigh-Alexandra Basha

High net worth, global citizens build their wealth across multiple borders by establishing international connections through businesses, families, properties, and investments. While international borders no longer confine global citizens of the world today, they do require sophisticated financial planning and exceptional product solutions. M International's insurance products and resources provide unique planning solutions for the challenges confronting global clients with and without U.S. ties.

Life Insurance Planning for International Clients with U.S. Ties

Life insurance death benefit proceeds on the life of a nonresident noncitizen are generally estate tax-free and life insurance cash values may be accessed on an income tax-free basis. However, life insurance owned by the nonresident alien (NRA) on the life of someone else is subject to U.S. estate tax. If death benefit proceeds are paid to a U.S. citizen/resident (U.S. person), they are includable in the recipient's estate.

Life Insurance Planning for International Clients without U.S. Ties

International clients are looking for solutions to their planning needs, which include income replacement, wealth transfer planning, creating liquidity at death, funding buy/sell, asset reallocation and key person coverage. For most cases, this planning does not need to be complex as it is not tax related (depending on the tax law of their country of residence). This may simplify trust and funding solutions.

Life Insurance as a Tool for International Estate Planning

Life insurance can provide solutions to complicated international estate planning situations for those clients with U.S. ties, some of which include:

1. Paying U.S. or foreign estate tax.
 - » Current U.S. estate tax is 40% plus up to 16% in some states (e.g., New York).
 - » Useful for both U.S. and nonresident insureds.
 - » Consider for NRAs investing in U.S. real property.
 - » Consider when a spouse is a non-U.S. citizen; no marital deduction.
 - » Consider for "covered expatriates" who are subject to the U.S. succession tax (IRC sec. 2801).
2. Eliminating undistributable net income (UNI) in a Foreign Nongrantor Trust (FNGT).
 - » UNI is a category of income that is subject to ordinary income tax rates (39.6% federal plus state plus 3.8% Net Investment Income Tax (NII)) plus a "throwback tax" that can be as high as 100% of the distribution.
 - » Trust assets held in a life insurance policy do not accumulate (UNI).
3. Paying the "throwback tax" on trapped UNI in an FNGT.
 - » Leverage the UNI and use part of it to pay the premiums.
 - » A MEC may be appropriate for distributing the trust assets more than one generation below.

Global clients face unique and complex challenges as they build their wealth across multiple borders. M Financial Group is committed to providing Member Firms with valuable knowledge and resources to address the multifaceted needs of their global clients.



A Primer on Life Insurance and Planning in a Global Market (continued)

4. Avoiding U.S. income tax during a period of U.S. residency by an NRA who will be in the U.S. for a short duration.
 - » Often use foreign annuity.
 - » Cash-in when NRA leaves the U.S.
5. To benefit from lower inheritance tax rates in some countries (e.g., 30% instead of 60% on proceeds passing to a non relative in France)
6. To protect assets from creditors (asset protection planning).

For international clients without U.S. ties who purchase international products (e.g. via M Financial Bermuda), many of the planning options listed above are unnecessary as the purchase of life insurance is not a tax play but rather a leverage solution for income, liquidity, etc.

What About Insurance Trust Vehicles and Reporting for Clients with U.S. Ties?

There is no requirement that the life insurance policy must be held in an Irrevocable Life Insurance Trust (ILIT), but it may be appropriate if the proceeds are passing to a U.S. person for whom it will be includable in his or her estate. A non-tax reason to use an ILIT is for creditor protection.

However, if the policy is held in an ILIT, then your client must be careful how the NRA funds the premiums in order to avoid a U.S. taxable gift (more than \$14,000 is a taxable gift if made in the U.S.).

Additionally, a U.S. person's known interest in a foreign insurance policy is a foreign financial asset and thus reportable on an FBAR and Form 8938 if the policy cash value exceeds the applicable threshold filing requirement.

Potential Landmines and Caveats for International Clients and Life Insurance

Clients should be careful if they hold life insurance in an ILIT in some countries (e.g., France and the U.K.) and be aware of the foreign life insurance reporting requirements as they relate to the U.S.

- The cash value of foreign life insurance policies is reportable as an account on an FBAR Disclosure (FinCen 114).
- Foreign life insurance is a foreign asset to be reported on Form 8938 (new as of 2011).
- Certain foreign life insurance policies (i.e., foreign life insurance wrappers) are treated as "passive foreign investment companies" (PFICs) and thus trigger interest charges reportable in the U.S. (also need to file Form 8621).
- Gifts to the ILIT are considered situated in the country where they are gifted (i.e., from NRA's bank account in the U.S.). NRA's gifts should be structured outside the U.S. to avoid triggering U.S. taxes and/or take advantage of applicable exclusions.

Other Notable Considerations for Life Insurance and Life Insurance Trusts

- When preparing a life insurance trust, ask your client if it should be a foreign or U.S. trust, either of which can limit trustee choices. Choosing the trust's beneficiaries is important as their residency determines the amount they will be taxed on any distribution from the trust.
- Determine if your client's estate is subject to forced heirship claims (i.e., in civil law jurisdictions, nationality, or citizenship heirship rules) that could disrupt the intent of the trust. In addition, consider the trust's tax clause. When advising clients with any foreign connection, check the provisions of any applicable tax treaties.
- Clients who qualify for Bermuda-based products would typically have policies owned by a revocable trust, a Personal Investment Company domiciled in neutral jurisdiction, or the insurance company's master purchasing trust in Bermuda.

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