ADVANCED MARKETS INSIGHT

Life Insurance: It's More Than Death Insurance

M Financial Group's Advanced Markets Insights are designed to help clients understand sophisticated planning strategies and their applications.

M Financial Group continues to lead the industry in insurance due care and client advocacy, providing valuable insight and anlysis that delivers significant value to clients.

Ultra-high net worth (UHNW) individuals and business owners are familiar with the value of life insurance and the usefulness of death proceeds, which, when policies are properly positioned, are not subject to tax. A life insurance death benefit:

- Generates immediate liquidity for highly illiquid estates.
- Pays federal and state estate taxes to transfer wealth intact.
- Creates special legacies or charitable bequests.
- Funds business continuation agreements and indemnifies a key person loss.

On the other hand, the lifetime benefits and living applications of permanent cash value life insurance are less recognized and greatly under-utilized.

Life Insurance as Valuable Property

For UHNW individuals and business owners with a long-term or permanent need for protection, permanent cash value life insurance—whole life, universal life (UL), index UL, or variable UL—should be regarded as a valuable and versatile asset. A permanent policy is an asset that can deliver many collateral benefits and uses over the years. The ultimate death proceeds provide security for families, preserve estates, and stabilize businesses.

Valuable Features

The unique features and tax characteristics of permanent life insurance deliver powerful benefits and permit user flexibility in a wide variety of financial planning applications:

- Tax-deferred cash value growth, often producing amounts greater than the annual premium payment during the period after initial policy years.
- Ability to efficiently access the growing cash values (on a FIFO basis in the case of a non-MEC policy) by withdrawing up to basis and using loans for any excess.[1]
- Exemption of policy values from the reach of creditors, amounts and limitations subject to certain federal laws and state insurance regulations.
- In the case of variable life, the ability to position premium dollars in stocks, real estate, and other equity sub-accounts without realizing current gains for tax purposes.

Variable life also provides the opportunity to perform portfolio re-allocation or rebalancing without current tax implications.

1 Income tax-free distributions are achieved by withdrawing to the cost basis (premiums paid) then using policy loans. Withdrawals will reduce the policy's cash value and may reduce the policy death benefit. Policy loans will reduce the policy's cash value and death benefit. This assumes the policy qualifies as life insurance and is not surrendered or allowed to lapse. If the policy lapses or is surrendered, the IRS will tax distributions received over the life of the policy and at termination that are in excess of total premiums paid. Amounts are based on assumptions and non-guaranteed crediting rates under the life insurance policy.

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Powerful Benefits

The foregoing economic features and tax treatment of permanent life insurance create possibilities for a range of lifetime planning applications for UHNW individuals and business owners:

- Immediate liquidity for illiquid individuals, trusts, or businesses at low or no-cost access through policy withdrawals or loans, or by pledging as collateral for commercial loans.
  - For example: education funds, new investment opportunities, or temporary credit stress.
- Asset diversification and balance for UHNW individuals and business owners who typically assume a high degree of risk in their overall portfolios and business ventures.
- A tax-managed asset for non-grantor irrevocable trusts with their severely compressed income tax brackets.
- A retirement income supplement, either on an annual systematic withdrawal basis, or an occasional ad hoc basis in the event of other, more market-based income sources being temporarily depressed.
  - There are no statutory contribution limits, and withdrawals (prior to age 59 ½) are not subject to a 10% penalty tax, as is the case with qualified retirement plan accounts.

Life Insurance Funding – Why Pay More Than The Minimum?

Although life insurance acquisitions made solely for death benefit and estate planning needs can be designed to achieve the minimum required sustainable premium, in many cases it makes more sense than ever in our high and rising income tax climate to deposit more than the bare minimum into this valuable and generative property—permanent cash value life insurance.

- Increased policy funding provides increased access to the value created by the product's tax treatment and cash value growth capability. At the same time, more funding reduces the policy's pure insurance cost charges, making the asset even more growth-efficient.
  - For example, this can achieve the asset diversification and tax-managed objectives of a high-bracket taxpayer such as a trust or individual high-income earner, whose interest, nonqualified dividends, and short-term investment gains are subject to rates as high as 43.4%, before state income taxes.
- Robust policy funding maximizes the life insurance policy's value as a ready source of liquid funds or collateral for active investors seeking new or time-sensitive situations and business owners seizing expansion opportunities.
- A healthy policy cash value cushion reduces the likelihood of lapse exposure in the event of a temporary cash flow constraint to pay new premiums.
- Heavier policy funding creates sufficient policy reserves to enable and empower the tax-efficient retirement income capabilities of a permanent cash value life insurance policy.
- An increased cash value reserve within the policy can support multi-purpose living benefits, such as long-term care features.

Summary

Life insurance is a valuable asset not just for surviving family members and business associates, but throughout the insured's lifetime. Infusing more premium dollars enhances all those lifetime possibilities. It's insurance…for life.

For More Information

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