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Communities of Coastal Georgia Foundation

Current Estate Planning

Innovative Strategies

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Agenda

I. Industry Update
   - A. Life Insurance Products
   - B. Life Insurance Carriers

II. Estate Planning in Current Environment

III. Select Life Insurance Strategies

IV. Criteria to Select a Life Insurance Advisor

Types of Life Insurance Products

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- Two basic types of life Insurance:
  - Term Insurance
  - Permanent Insurance
    - Whole Life (WL)
    - No-Lapse Guarantee Universal Life (NLG)
    - Universal Life (UL)
    - Variable Universal Life (VUL)
      - Private Placement Variable Universal Life (PPVUL)
    - Index Universal Life (IUL)

General Product Descriptions

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- **Term** – Fixed premium for a period of years. No cash value. 10, 15, and 20 years most common durations. Can be converted to permanent coverage depending on the carrier.
- **Whole Life (WL)** – Policy premiums must be paid. Designed to grow Cash Value to eventually equal Death Benefit. Very rigid design. Dividend is not guaranteed.
- **No Lapse Guarantee Universal Life (NLG)** – Permanent coverage where death benefit is guaranteed if premiums paid timely. Builds little (or no) cash value. Limited flexibility.
- **Universal Life (UL)** – Permanent coverage designed to remain in-force for a specified period of time (usually life). Very flexible premium and duration design. Crediting rate is declared by carrier subject to minimum crediting rate guarantee.
- **Indexed Universal Life (IUL)** – Permanent life insurance where the crediting rate for the cash value account has a cap and floor. Crediting rate is based on an equity index. Fastest growing product segment in the industry, and highly complex.
- **Variable Universal Life (VUL)** –Permanent life insurance that allows the cash value to be invested in separate accounts (sub-accounts that are akin to mutual funds). Performance is not guaranteed. Highly flexible product.

Life Insurance Product Issues

- Who controls performance?
  - Carrier – General Account policy
  - Policyowner/Insured – Separate Account policy
- Why important
  - Higher performance (rate of return)
  - Lower premium required
  - Possible higher risk

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Importance of Active Management

- Life insurance illustrations and performance are not guaranteed
- Product performance will change over time
- Actions may be required to meet the original insurance goal
- Different product types have different risks and guarantees which impact product performance
- The insurance marketplace continues to evolve
  - More product options
  - Better pricing tied to improving mortality
  - Complete transparency and extreme flexibility are available—important to high net worth clients
- Every life insurance portfolio needs to be reviewed

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Life Insurance Carrier Issues

- Low Interest Rate Environment
  - Interest rate pressures—carriers may be "reaching" for yield
  - Strained profit margins
- Reserve Issues
  - Regulation driven
  - Higher price for guarantees
- Innovation
  - Product
  - Underwriting
  - Technology

Estate Planning in Current Environment

- Stability of Estate Transfer Tax rules
- Large exemption – $5,430,000 in 2015
- Small percentage of families exposed to Transfer Tax
  - Clients less like to focus on non-Tax issues
  - Clients less likely to engage advisors
- Cannot ignore GST Tax
- Increased relative importance of income tax issues
- Undoing prior planning strategies
  - Importance of flexibility—planning strategies and life insurance portfolios
  - Life insurance policy valuation issues
    - "Old trust" to "new trust"
    - Company to insured

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Potential Options For Consideration

Options for those whose Life Insurance needs have changed:

- Drive greater efficiencies via reducing premium or paying up the policy
- Discontinue premium payments and let the policy last as long as there is cash value (CSV) to support it
- Surrender the policy – examine the IRR before doing so and compare to other investment alternatives
- Annuitize – IRC Section 1035 exchange into an annuity
- Convert the policy to a hybrid life insurance / long term care product - qualifies as a tax free exchange
- Sell into secondary market

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Most Common Uses

- Most Common Uses of Life Insurance:
  - Family protection
  - Estate protection
  - Family equalization
  - Business planning
  - Asset allocation
  - Income tax planning

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Case Study #1
Concentrated Stock Position

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Concentrated Stock Position

- Husband (69) and Wife (65) – both healthy
- $30 Million Taxable Estate
  - Mostly Coca-Cola stock (inherited from wife's parents)
  - Potential $13.5 million estate tax liability*
- Estate Tax Liability Funding Alternatives
  1. Liquidate Coke stock
     a) Sell $13.5 million of stock at 2nd death
     b) No (or little) capital gain tax liability because of stepped-up basis
     c) May be forced to liquidate during a depressed market/economy as estate only has 9 months to raise funds

* Based on 2009 rules

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Concentrated Stock Position

2. Wealth Replacement Strategy

   a) Fund some of the estate tax liability with proceeds from a 2nd-to-die life insurance policy
   b) Policy owned by Irrevocable Life Insurance Trust (ILIT), excluding death benefit proceeds from taxable estate
   c) Private loans made from Grantors to ILIT support the annual premiums of the life insurance policy

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Concentrated Stock Position

- Life Insurance Portfolio
  - Male / 69 & Female / 65
  - $13.5 million face amount
  - Future death benefit increases based on premiums paid (face amount + cumulative premiums paid)
  - $241,773 annual premium

Year	Cumulative Premium Paid	Death Benefit	Internal Rate of Return	
			Unadjusted	Income Tax Adjusted [1]
15	$3,626,595	$17,126,595	17.8%	24.7%
20	$4,835,460	$18,335,460	11.5%	15.9%
25	$6,044,325	$19,544,325	8.2%	11.3%
30	$7,253,190	$20,753,190	6.1%	8.5%

[1] Tax-equivalent return assumes 41% ordinary tax rate / 21% capital gains tax rate and investment portfolio of 2/3 capital gain returns and 1/3 ordinary income items.

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Concentrated Stock Position

- Wealth Replacement Strategy
  - Annual loans of $241,773
  - 2.70% mid-term AFR (increasing to 4.0% by year 15)
  - Loan interest is accrued
  - Assume no growth in estate

Year	Net to Heirs with Wealth Replacement Strategy [1]	Net to Heirs without Strategy	Increase
15	$29,527,405	$16,500,000	$13,027,405
20	$29,002,579	$16,500,000	$12,502,579
25	$27,246,192	$16,500,000	$10,746,192
30	$27,208,075	$16,500,000	$10,708,075

[1] 'Death Benefit Proceeds' plus $30 million taxable estate less 'accumulated premiums paid' (net of a 45% estate tax liability).

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Case Study #2
Leveraging the Lifetime Exemption

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Leveraging Lifetime Exemption

- Couple completed wealth transfer planning in the 2012 rush
- Used $10 Million exemption—transferred significant wealth
- No additional planning or transfers since then
- 2015 Lifetime Exemption = $5,430,000
  - Increased annually by inflation index
  - Assuming 2% annual growth, projected annual increases are:

2012 – 2015 *	$430,000
2016	$109,000
2017	$111,000
2018	$113,000
2019	$115,000
2020	$118,000
2021	$120,000

**Actual increase since 2011*

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Leveraging Lifetime Exemption

- Husband (60) & Wife (60) – both healthy
- The increased annual exemption will:
  - Acquire $8,000,000 2nd-to-die life insurance with a seven pay premium
  - Protect a taxable estate of $20,000,000 from Federal estate tax erosion

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Leveraging Lifetime Exemption

- Consider using the annual exemption for both spouses
  - \$16,000,000 of 2nd-to-die life insurance with a seven pay premium
  - Protects a taxable estate of \$40,000,000 from Federal estate tax erosion
- If one spouse dies within seven years:
  - Pay lower premiums for more years with survivor's exemption
  - Reduce the policy face amount
  - Make annual gifts (if available & Trust allows)
  - Pay gift tax
  - Make private loans to Trust

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Case Study #3
Charitable Planning

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Charitable Planning

- Husband (65) & Wife (65) – both healthy
- Strategy: Give Now & Replace Wealth with Life Insurance
  - Gift $5 million to Charity now
  - Benefit from "joy of giving" and possible input on use of funds
  - Income tax savings of $2,250,000 assuming a 45% marginal income tax rate
  - Income tax savings allocated to life insurance policy to "replace" wealth

❑ Life Insurance Solution
  - 2nd-to-die coverage
  - $562,500 annual premium for 4 years ($2,250,000 total)
    - Avoid Modified Endowment Contract (MEC)
  - $11,250,000 death benefit

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Charitable Planning

Year	EOY Age	Gift to Charity	Income Tax Savings (@ 45%)	Life Insurance Policy to Benefit Heirs: Annual Premium (non-MEC)	Cash Surrender Value @ 4.30%	Death Benefit	Tax-Free IRR (Death Benefit to Premiums)
1	66	(5,000,000)	2,250,000	(562,500)	468,576	11,250,000	1900.00%
2	67	0	0	(562,500)	953,644	11,250,000	300.00%
3	68	0	0	(562,500)	1,455,640	11,250,000	131.13%
4	69	0	0	(562,500)	1,979,404	11,250,000	76.27%
5	70	0	0	0	1,987,074	11,250,000	53.41%
6	71	0	0	0	2,046,498	11,250,000	40.73%
7	72	0	0	0	2,100,540	11,250,000	32.79%
8	73	0	0	0	2,148,236	11,250,000	27.38%
9	74	0	0	0	2,191,597	11,250,000	23.48%
10	75	0	0	0	2,230,654	11,250,000	20.54%
15	80	0	0	0	2,417,383	11,250,000	12.59%
20	85	0	0	0	2,570,462	11,250,000	9.06%
25	90	0	0	0	2,680,973	11,250,000	7.08%
30	95	0	0	0	2,263,539	11,250,000	5.80%
35	100	0	0	0	608,892	11,250,000	4.92%

Results: Immediate $5,000,000 support to Charity and $11,250,000 to heirs at 2nd death.

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Case Study #4
Planning with IRA Assets

Planning with IRA Assets

- Husband (75) & Wife (75) – both average health for age & gender
- IRA
  - Current balance: $1,000,000
  - Assumed annual growth rate: 5%
- Tax Rates
  - No estate tax liability anticipated
  - Marginal income tax rate: 40%
  - Marginal income tax rate (children): 40%
    - Built-in income tax liability on IRA is $400,000
- Life Insurance Design

  $400,000 death benefit payable at 2nd death
  - $10,250 annual premium

Planning with IRA Assets

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Age	Estimated Annual MRD	IRA Value (EOY)	Built-In Income Tax Liability	WITHOUT Life Insurance: After-Tax Net to Children	WITH Life Insurance: Life Insurance Proceeds	WITH Life Insurance: After-Tax Net to Children	WITH Life Insurance: % Increase to Children
75 / 75	43,668	1,004,148	(401,659)	**602,489**	400,000	**1,002,489**	66%
80 / 80	53,546	995,146	(398,058)	**597,087**	400,000	**997,087**	67%
85 / 85	63,795	924,387	(369,755)	**554,632**	400,000	**954,632**	72%
90 / 90	71,560	781,433	(312,573)	**468,860**	400,000	**868,860**	85%
95 / 95	72,079	575,194	(230,077)	**345,116**	400,000	**745,116**	116%
100 / 100	61,746	343,614	(137,446)	**206,169**	400,000	**606,169**	194%

- An annual allocation of $10,250 into a $400,000 life insurance policy can protect the absolute value of the IRA from income tax erosion in the early years.
- In the later years, the life insurance policy can enhance the amount transferred to children by providing more liquidity than required from projected income tax liability.

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Selecting an Insurance Advisor

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- Independence
- Client problem solver—not Carrier product provider
- Access to best product
- Knowledge, access to information, ability to influence Carrier
- Carrier selection methodology
  - Product performance: projected, sustainability, and in-force management
  - Service capability
  - Financial strength
- Underwriting process
- Service capability of Insurance Advisor

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Disclosures

Variable life insurance products are long-term investments and may not be suitable for all investors. An investment in variable life insurance is subject to fluctuating values of the underlying investment options and it entails risk, including the possible loss of principal.

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