Recalibrate & Replace

Situation

We were asked to review two variable life policies owned by a High Net Worth client and his wife for many years. They were not sure how well funded the policies were and had a different perspective on the value of them from when they were originally purchased.

Circumstance

The client has a successful business and was just surpassing a $10 million net worth. He and his wife had other insurance coverage in place including some business continuity protection. They no longer needed the variable life policies for their original intent and were considering cashing them in. They already purchased long-term care protection and with their success, were now focused on estate tax and legacy planning.

Problem

Their current policies each had a gain and were owned inside their taxable estate. After auditing their policies (under current assumptions & a reasonable rate of return), we found them to be at low risk of implosion but one of them could need additional funding down the road. The other was funded well enough to potentially cause the level death benefit to increase, but between both policies it was unlikely they would pay more than $500,000 total to their heirs. The policies were also not guaranteed past the next 10 years.

Solution

We showed the client how we could annuitize the cash value from their existing policies over a 10-year period to fund annual exclusion gifting to an ILIT owned $1 million dollar second-to-die policy. You can't conduct a 1035 exchange from individual policies to a second-to-die policy and thus the 10-year only annuity helps spread the tax over the next 10 years. The new policy was also guaranteed for life, so the client decided to pursue this option.

Takeaways

- Reviewing both the performance and purpose of a policy is important.
- Estate planning is not about what you make, it is what they keep that matters. Life insurance can often be an unbeatable estate leverage tool when compared fairly and owned properly.
- Although we don't know when the second death will occur, when it does; we will know the net return at that time. If the second death occurs at 92 the return is 5.26% net.
- For an additional $3,000 (out-of-pocket) for the next 10 years, they will more than double what they leave behind from their existing policies. They will have also removed both federal and state estate tax exposure from this asset.

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The Numbers

- Deposit the $173,347 cash value from their existing variable life policies into a 10 Year Only SPIA
- SPIA generates a net income of $17,653
- Clients pay $3,087 out-of-pocket per year for the next 10 years into a $1Mill Second-to-die policy owned by an ILIT.
- They leave $1M to their heirs at the second death, federal & estate tax free.

Year	Combined		Survivor GUL	
	VUL Death Benefit		$20,740 10-Pay	
	Gtd (0%)	Projected (6%)	Death Benefit	IRR
1	$ 450,000	$ 450,000	$ 1,000,000	10748.44%
5	$ 450,000	$ 450,000	$ 1,000,000	88.17%
10	$ 350,000	$ 450,000	$ 1,000,000	27.58%
15	$ -	$ 465,847	$ 1,000,000	15.26%
20	$ -	$ 488,288	$ 1,000,000	10.40%
25	$ -	$ 527,617	$ 1,000,000	7.85%
30	$ -	$ 227,303	$ 1,000,000	6.30%
35	$ -	$ 286,770	$ 1,000,000	5.26%
40	$ -	$ 358,221	$ 1,000,000	4.51%
A100	$ -	$ 417,151	$ 1,000,000	4.15%

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