The Wealth Counselor

A monthly newsletter for wealth planning professionals

How and Why Life Insurance Still Matters in Estate Planning

A frequently overlooked aspect of a client's life insurance is proper alignment with estate planning goals. Between the typical set-it-and-forget-it mentality and a simple beneficiary approach many people take, a neglected life insurance policy often fails to achieve the goals that initially led to the purchase of the policy.

But, you can help. You, as the trusted financial advisor, and us, as the estate planning attorney, can thoroughly review your client's life insurance needs and policies. You may be able to recommend modifications or new policies to address vulnerabilities, and we can ensure that the ownership of the policy and death benefit are properly aligned to achieve your clients' estate planning goals. By building deeper and broader relationships with your clients, you can grow your own business through referrals, earn commission on any newly written life insurance, and, potentially, undertake management of assets when the policies pay out.

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The Duvall Law Firm believes in taking the "team approach" to estate & business planning. Providing effective, responsible service to our clients leads us to build and maintain relationships with clients' professional advisors. Cooperation is the cornerstone of our relationships with both advisors and the clients we serve together.

What can go wrong with life insurance?

Many people fail to integrate their life insurance policies into their estate planning effectively.

Here are just a few of the many things that can go wrong:

1. A client may think their life insurance is entirely separate from their other assets. As a result, they fail to adequately account for this asset in their estate plan, missing opportunities to provide for their family.
2. A client may have an old, underperforming policy that follows dated mortality tables, bears higher administrative costs, or yields lower interest than a more current policy would. There has been so much change in the financial services and insurance industry over the years that "old" policies certainly need a fresh look.
3. A client may own life insurance inside an Irrevocable Life Insurance Trust or

ILIT. Depending on the client's needs, age, health, and financial status, the ILIT itself may no longer be necessary. ILIT-owned policies should also be reviewed, as they may need to be replaced by a new policy.

4. A client may have outdated or non-existent beneficiary designations. Common mistakes include naming a deceased person, a former spouse, a minor child or grandchild, or omitting children born after the policy was issued. Integrating life insurance into a clients' estate plan can resolve these issues and more.

Tools for life insurance estate planning

The good news for your clients, and for you, is that a full review of the estate plan will often reveal these vulnerabilities so you can correct them before any adverse outcomes occur. Of course, the solution will differ from client to client based on the size of the estate, the current ownership and beneficiary structures, and other factors.

The 1035 Exchange

Typically, when a permanent or universal life insurance policy is cashed out, the proceeds count as taxable income. However, a 1035 Exchange, named after the applicable section in the tax laws, enables your client to trade in a less-than-ideal "old" life insurance policy for a "new" life insurance policy without adverse income tax consequences. Depending on the size and complexity of your client's estate plan, this simple switch may be all that's needed at the moment; at other times, you'll use it simultaneously with other strategies.

Obtain a Completely New Policy or Convert a Term Policy

If your client has a term life insurance policy, it might make sense to get an entirely new policy. Of course, a client's health is a significant factor here and that alone might be a reason to convert an existing term policy into a permanent policy, if a conversion feature is available. Some insurers even allow for the addition of long-term care riders or other "lifetime" access features that either weren't available at all or weren't widely available in the past.

Irrevocable Life Insurance Trust (ILIT)

Life insurance death benefits are considered part of a decedent's estate and are therefore subject to estate tax. The proper design, funding, and implementation of a special trust designed to own life insurance, known as an Irrevocable Life Insurance Trust or ILIT, can save estate taxes. Unfortunately, many people consider these trusts for estate tax reasons only, but the robust asset protection and asset management consolidation for beneficiaries can be reason enough to create one of these trusts.

Stan Miller, a principal of WealthCounsel and estate planning attorney at ILP + McChain Miller Nissman, summarizes the asset management benefits of trusts:

"In my experience, wealth that is aggregated and managed will grow and provide a lasting benefit to a family. On the other hand, wealth that is divided and distributed

dissipates. It simply doesn't create a long-term benefit. Life insurance, for many people, creates instant wealth that, when properly managed inside a trust, can provide lifelong benefits to your spouse, children, and even grandchildren."

The importance of ongoing insurance review and management

The best way to help keep your clients' life insurance component current is through periodic review and continuous management. Here are some examples of what this review process can look like:

- If you have a client who has no life insurance, now is the perfect time to strategize with him or her and get an appropriate policy in place.
- As a client's wealth continues to grow, the amount of life insurance may need to adjust. (For those clients with taxable estates, the life insurance death benefit might actually be used to provide liquidity to pay federal or state estate taxes. In these cases, we'll work with you and the clients to ensure the overall plan design makes these funds available without causing any estate tax problems.)
- If your client has an ILIT, then he or she cannot be the trustee. Otherwise, the estate tax benefits are nullified. You may either be able to fill that role or work alongside a family member appointed to that position. An ILIT that hasn't been maintained well may not be effective either, so we should coordinate a trust review with you and your clients in addition to reviewing the insurance policy.
- As your client's financial and estate planning needs change, ongoing monitoring ensures that a client's life insurance plan adapts to keep pace.

Reinforce to your clients that life insurance is part of their wealth and wealth that isn't managed tends to dissipate. By offering your review and management services now, you are building a relationship and helping your clients and their beneficiaries preserve wealth for the future.

We're here to assist.

A well-structured life insurance component can be a welcome addition to any estate plan. But don't use life insurance in a vacuum – work with us to coordinate it with your clients' estate plans. Our team can help you provide strategic estate planning services for your clients. Give us a call or email us with your questions at any time.

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