CRESCENT WEALTH MANAGEMENT

Advanced Design Strategies

Life Settlements

Overview

A Life Settlement is the sale of a life insurance policy for an amount greater than its cash surrender value. The proceeds are often used to purchase other financial products, including more cost effective life insurance.

Prospect Profile

Age: At least 70, with a life expectancy of 12 years or less

Status: High net worth seniors with a minimum $250,000 life insurance policy issued at least two years ago.

Concerns: Client needs a means to tap into unrealized assets from an existing policy or the current policy is no longer needed for its original purpose.

Annuity Arbitrage

Overview

This strategy may assist an older client in achieving both income and/or wealth transfer goals by selling assets and reinvesting the proceeds in a Single Premium Immediate Annuity (SPIA). The client retains some (or none) of the SPIA income and gifts the balance after taxes to an Irrevocable Life Insurance Trust (ILIT) to pay premiums on a life insurance policy for the benefit of the heirs.

Client Profile

Age: 70 to 85 and insurable. The strategy can be effective with clients younger than 70 and older than 85, however, the "arbitrage" may be reduced.

Concern: Needs more after tax income and/or wants to increase family inheritance.

Suitable Assets: Assets that can be sold with little or no capital gain tax consequences, for example, CDs or bonds or existing deferred annuities that can be converted to a single premium immediate annuity (SPIA).

Tax Status: Works best at highest income and estate tax brackets

Other: Individual should have other significant sources of liquidity since this strategy consumes liquidity.

What is Premium Financing?

Premium financing is a strategy intended to assist clients obtain life insurance for which they have an established need. Typically, premium financing is a fair market loan arrangement between a commercial lender and an irrevocable life insurance trust (ILIT) where the lender loans the premiums for a life insurance policy on the client's life to the ILIT. In that case, the gift to the ILIT is equal to the amount of loan interest charged – not the entire policy premiums. As a result, the client is able to acquire the death benefit needed with little or no gift tax impact.

With regard to the specific loan terms, the policy usually serves as the primary collateral for the loan. During the early years of a policy, cash surrender values are generally less than premiums paid. As a result, the client is typically required to provide additional collateral. Loan interest can be paid annually or deferred for a period of time. Loan principal, including any accrued interest, may be repaid from the life insurance proceeds or from other sources during the client's lifetime. Potentially, a return of premium rider can be used to repay the premium loan without diminishing the death benefit needed. In summary, premium financing makes great economic sense when there is a positive arbitrage between the policy's internal rate of return or the trust's investment return and the loan interest rate.

What is Private Financing?

Typically, private financing is a fair market loan arrangement between the client and an irrevocable life insurance trust (ILIT) where the client loans the premiums for a life insurance policy on the client's life to the ILIT. In that case, the gift to the ILIT is equal to the amount of loan interest charged – not the entire policy premiums.

Loan interest can be paid annually or deferred for a period of time. As a result, the client is able to acquire the death benefit needed with little or no gift tax impact. Loan principal, including any accrued interest, may be repaid from the life insurance proceeds or from other sources during the client's lifetime. Potentially, a return of premium rider can be used to repay the premium loan without diminishing the death benefit needed.

In summary, private financing premiums can make great economic sense when there is a positive arbitrage between the policy's internal rate of return or the trust's investment return and the loan interest rate.

What Is Private Split Dollar?

Private split dollar is a premium sharing arrangement between the client and an irrevocable life insurance trust (ILIT). Client enters into a non-equity collateral assignment agreement with an ILIT wherein the client agrees to pay the full annual premium in exchange for a restrictive collateral assignment in the policy, which entitles the client to be repaid the greater of their premiums paid or the total cash value of the policy at some point in the future. As a result, the client is able to acquire the death benefit needed with little or no gift tax impact. The collateral assignment may be satisfied with life insurance proceeds or from other sources during the client's lifetime. Potentially, a return of premium rider can be used to satisfy the collateral assignment without diminishing the death benefit needed. In summary, private split dollar can provide a tax-efficient and cost-effective strategy to pay for life insurance.

Charitable Remainder Trust (CRT) With a Wealth Replacement Trust

A Charitable Remainder Trust (CRT) is an irrevocable trust with significant income tax advantages. It is referred to as a split-interest trust because it has both charitable and non-charitable beneficiaries. It also serves dual purposes: (1) to provide you with a stream of income, and (2) to have the balance of that asset eventually go to your favorite charity. A Wealth Replacement Trust (WRT) is an irrevocable life insurance trust that has significant estate tax and legacy benefits. It allows for the purchase of life insurance inside of the trust, thereby keeping the insurance proceeds out of your taxable estate. The beneficiaries of this trust, however, are your children so the insurance proceeds can "replace" the assets that you donate to charity using the CRT technique. The premiums for the insurance are paid using a portion of the income stream that you receive from the CRT leaving you with no out-of-pocket expense. As a result, the assets used to fund the CRT can be used to provide you with an income stream and to ultimately benefit charity, all without reducing the legacy you leave to your children and heirs.

What Does Intentionally Defective Grantor Trust (IDGT) Mean?

An estate planning tool used to freeze certain assets of an individual for estate tax purposes, but not for income tax purposes. The intentionally defective trust is created as a grantor trust with a purposeful flaw that ensures that the individual continues to pay income taxes, as income tax laws will not recognize that assets have been transferred away from the individual.

For estate tax purposes, however, the value of the grantor's estate is reduced by the amount of the asset transfer. The individual will "sell" assets to the trust in exchange for a promissory note of some length, such as 10 or 15 years. The note will pay enough interest to classify the trust as above market, but the underlying assets are expected to appreciate at a faster rate.