

Key Wealth Institute

Four Ways to Use Life Insurance in Wealth Management Plans*

Article produced by the Key Wealth Institute's team of experts

For high-net-worth families and individuals, life insurance can provide benefits that go well beyond replacing income to support beneficiaries when you pass away. When included as part of a comprehensive estate plan, life insurance can provide liquidity to pay estate taxes, allow beneficiaries to retain ownership in important assets like family businesses and real estate, equalize inheritances among survivors, maximize your wealth, and secure your legacy.

1. Estate tax liquidity

Above certain amounts, the U.S. government imposes an estate tax on the transfer of property at death. In addition to federal taxes, a number of states impose an estate tax or inheritance tax, as well.

These taxes, along with other expenses, must be paid soon after death. However, high-net-worth individuals and families often own special or illiquid assets such as a business or real estate, making it difficult or impractical to convert them quickly into cash.

Life insurance has historically been an attractive asset to help pay for estate taxes and provide estate liquidity. One of the most common ways of incorporating life insurance into a wealth transfer plan is by using it in conjunction with an irrevocable life insurance trust (ILIT), which offers advantages that are not available with outright policy ownership by an individual.

In an ILIT, the trust is the owner and beneficiary of an insurance policy on your life. Unlike a policy you own directly, this allows the ILIT to receive the death benefit free from estate taxes and provides the funds needed for estate taxes and other costs.



2. Estate equalization

In creating an estate plan, one of the most important decisions you make is determining how much each heir will receive and what form the inheritance will take.

Dividing the assets equally among heirs may be the desired outcome, but there are situations where this can be difficult due to the assets involved.

For example, leaving certain assets such as a family home to multiple heirs can be impractical. A family business can also present complications, especially when some family members are involved in the business while others are not. Leaving the business to those who are running it makes sense, but what happens to those who are not engaged in the company's operations? If the business represents the bulk of the estate's value, other assets may not be of sufficient value to treat every heir equally.

Life insurance can be used to ensure inheritances are equalized and to address the challenges that come with assets that are difficult to divide. You could purchase a permanent life insurance policy or your ILIT can purchase the policy if estate taxes are a concern. The proceeds from the death benefit can then be used to ensure heirs receive the inheritance you wish them to have.

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3. Wealth accumulation and protection

Life insurance is an important consideration for any family, particularly if there is a large income disparity among family members. In these situations, the tax-free death benefit can protect your family when they need it most.

However, when properly designed and funded, permanent life insurance can offer ways to protect your family as well as enhance retirement income in a tax-advantaged vehicle.

Cash value life insurance policies accumulate a cash balance inside the policy. This cash balance grows on a tax-deferred basis, providing policyholders an option to grow their wealth in a tax-favorable manner. In addition, cash balances held within insurance contracts may be afforded creditor and liability protection by the state in which the policy was purchased.

A permanent life insurance policy provides flexibility to access the policy's cash value with tax-favored distributions, as well. Policyholders can access potential policy cash value via tax-favored loans and withdrawals to supplement retirement income.

This solution is often used by individuals who wish to contribute beyond limits in traditional retirement savings vehicles, like 401(k)s and IRAs.

4. Securing a legacy or enhancing a charitable gift

Life insurance policies can also be used to ensure charities that are important to you — including a family foundation — are not only funded but that donated wealth is replaced for family members.

A popular vehicle for estate planning purposes is a wealth replacement trust, which combines a life insurance policy, an ILIT, and a charitable remainder trust (CRT) to replace assets donated to a nonprofit. In a wealth replacement trust, you use income from the CRT to pay premiums on the life insurance policy, which is owned by the ILIT. You may choose to replace all or a portion of the property that will go to the charity via the CRT.

Using a wealth transfer trust has valuable tax benefits. The charitable income tax deduction can be used to fund the life insurance policy, which effectively allows you to replace donated assets at a discount. And since the life insurance policy is owned by the ILIT, the policy's proceeds can avoid estate taxes.

Evaluating life insurance as part of your estate plan

Life insurance can play an important role in your estate planning strategy:



Liquidity



Help beneficiaries
retain ownership
in important assets



Equalize
inheritances



Enhance wealth
accumulation



Secure
your legacy

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To learn more about how life insurance can align with your goals, contact your advisor or a Key Private Bank Wealth Protection Strategist.*

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