Life insurance requires regular review

Strategy snapshot

The need

You've already taken the important step of setting up your estate plan using life insurance. Properly structured and funded life insurance policies can be used to help meet a variety of objectives, such as:

1. Providing tax-free proceeds to beneficiaries with proper planning[1]
2. Supplying a cash death benefit for taxes, or living expenses while your estate is settled
3. Avoiding the time and expense of probate

Although your estate plan is in place, it is important that you not forget about your insurance policies. They should be reviewed every 1-2 years to ensure they are still meeting the goals you've established for you and your family. Changes to your family or financial circumstances, as well as insurance industry changes over the past several years support the regular review of your policies.

Hypothetical situation

Paul and Margaret set up their estate plan ten years ago. At that time, they established an irrevocable life insurance trust (ILIT) funded by two second-to-die policies on their lives from two different companies. One policy was a participating whole life policy; the other was a universal life policy. The couple has diligently made gifts to the trust each year to cover premium payments and the trust is in good shape. However, no one—including the trustee—has reviewed the life insurance policies since the trust was established.

At the request of their Financial Advisor, Paul and Margaret contacted the ILIT's trustee and asked to have both policies reviewed. After a thorough analysis, it was determined that neither policy was performing as expected. The participating whole life policy had experienced dividend cuts over the last ten years. The universal life policy was being credited more than 5% less than assumed by the illustration upon which the policy was purchased—and it would now require premiums be paid for an additional twelve years.

The result[2]

The review included an evaluation of other policies currently available in the marketplace, taking into account price and Paul and Margaret’s current insurability. Paul quit smoking about seven years ago; as a result, he and Margaret were pleased to discover that Paul is now eligible for preferred non-smoker rates where the previous policies had each been issued at a more costly smoker's rate. Paul had never thought of informing his insurance companies of this positive change in his health. With new policies and improved underwriting ratings, Paul and Margaret’s trust now owns life insurance with an approximately 20% higher death benefit and a reduced period of premium payments.[3]

Potential benefits to you

By having your life insurance policies reviewed regularly, you can:

- Ensure your life insurance coverage is up-to-date and consistent with your existing goals/objectives
- Evaluate older policies against other competitive products in the marketplace
- Avoid any potential lapses in coverage

Insurance industry changes support policy reviews

- Cost of coverage has come down with average lifespan increases
- New, more efficient policies have been introduced the past several years
- Policies with new features are now available (e.g., secondary guarantees for Universal Life products, long-term care riders, etc.)
- Existing polices purchased during higher interest rate environments may now require additional or increased premium contributions in order to stay "in-force"

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1. Properly structured and funded within an Irrevocable Life Insurance Policy (ILIT).
2. This example is hypothetical, actual results will vary.
3. This document is not designed to encourage life insurance replacement, life insurance is medically underwritten. A change in policy may require a medical examination. You should not cancel your current coverage until your new coverage is in force. Surrender charges may be due on an exchange of one contract for another. Surrenders may also be taxable. You should consult your own tax advisors regarding tax liability on surrenders.

The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (Act) impacts the federal gift, estate and generation skipping transfer tax (together referred to as "transfer tax") through 2012. Among other changes, the Act temporarily establishes maximum exemption amounts of $5,000,000 per person for transfer tax purposes, establishes a maximum transfer tax rate of 35% and provides for portability of the estate tax exemption between spouses. These changes, however, are only in effect through December 31, 2012. Unless Congress enacts new legislation, on January 1, 2013, the transfer tax laws will revert back to the laws (e.g. exemption amounts of $1,000,000 and generally 55% maximum tax rates) that were in effect in 2001. At this time, it is not clear what steps, if any, Congress will take to revise the transfer tax laws for years beyond 2012. Future changes in transfer tax exemption amounts and transfer tax rates may impact the appropriateness of any transfer tax planning strategy or product sale. Clients need to understand that tax law is always subject to interpretation and legislative change.

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