EQUITABLE

Cash value life insurance

How to plan for tax-efficient retirement income

The benefits of using a 7702 cash value life insurance to manage your tax brackets in retirement

Just 20 years ago, 60% of Fortune 500 companies offered pensions as a source of retirement income for American workers. Today, only 16% of those companies offer pensions to new hires,[1] forcing workers to save in other ways. Personal savings now fill that void, with increased reliance on IRAs and 401(k) plans, many of which will be subject to taxation at some to-be-determined future rate.

Three types of tax buckets

When you're talking about taxes, there are three buckets, or types of investments —

- Tax-deferred accounts.
- Taxable holdings.
- Those generating tax-free income at retirement.

Getting the "right" retirement income mix

To create tax-efficient income in retirement, you will therefore need to have a mix of these three types of investments:

Taxable investments

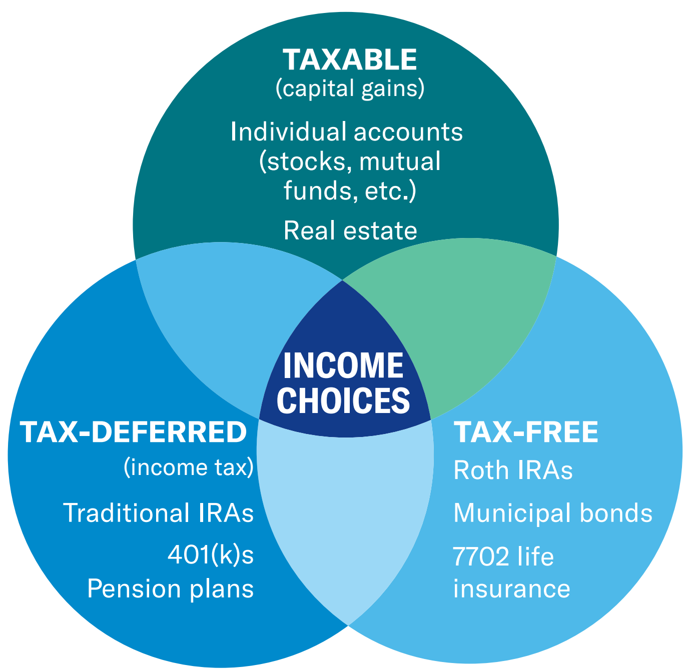
Taxable investments include assets, such as stocks and mutual funds, as well as real estate, including the primary residence. There is no tax deduction up front, and when the assets are sold, they are generally subject to capital gains tax. Please check with a tax advisor for your personal circumstances.

Tax-deferred investments

Tax-deferred investments include defined benefit (pension) and defined contribution plans, plus other traditional retirement savings vehicles, such as 401(k)s and IRAs. You may receive a tax deduction when contributions are made, and the assets grow tax-deferred, but are subject to ordinary income tax when withdrawals are made at retirement. There is also a possible 10% IRS penalty on any withdrawals before owners turn age 59½.

Tax-free assets

Tax-free assets include Roth IRAs, municipal bonds and cash value life insurance. Withdrawals (and loans from cash value of a life insurance policy) are not subject to either income or capital gains tax.[2]



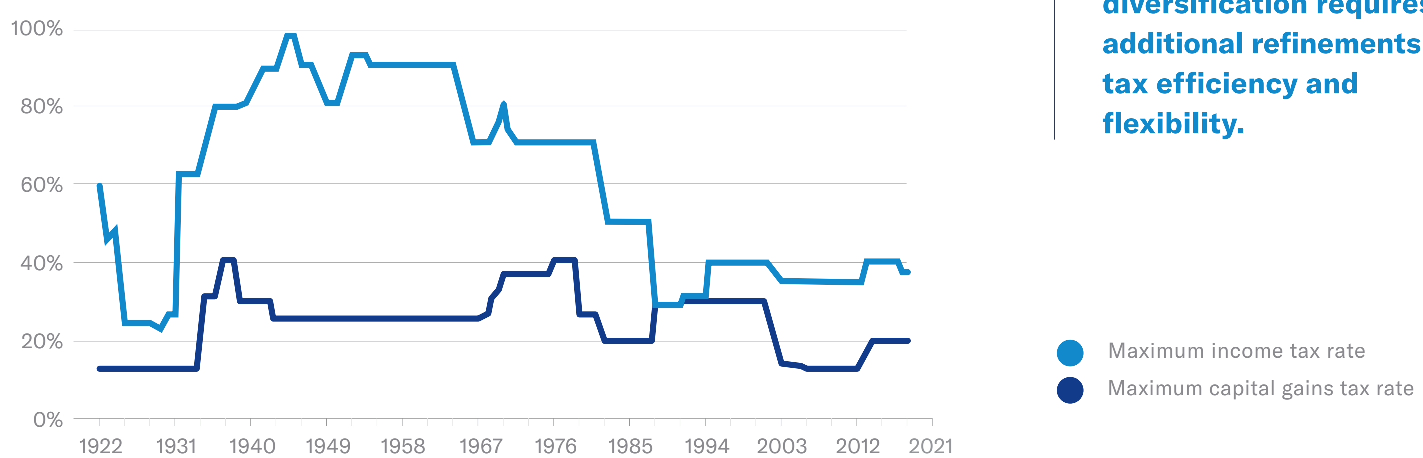
It's important to plan now to manage all the various assets in these three buckets and to strategize withdrawals in retirement to create the maximum benefit. Your plan needs to consider current and future tax situations, your financial goals and the structure of each asset.

The uncertainty of future tax rates

It can be challenging to plan for tax efficiency when you're not sure what tax rates will be in the future. After all, the capital gains tax and income tax rates have fluctuated over the past 100 years and most likely will continue to do so.

Based on the uncertainty of our applicable tax rates in the future, retirement income planning focused on tax management and diversification requires additional refinements — tax efficiency and flexibility.

Capital gains and income tax timeline (1922-2019)



Consider 7702 cash value life insurance

For those who qualify for additional life insurance, adding a 7702 life insurance policy with cash value to a retirement portfolio may provide favorable tax benefits that can enhance retirement planning. Some of the hurdles associated with permanent life insurance, including insurance charges and other fees, can be mitigated with careful design and planning — allowing you to manage your tax bracket through tax-free distributions,[2] rather than drawing income from investments that are fully or partially taxed during retirement.

What is IRC §7702?

For all life insurance policies issued after 1985, the government defined what constitutes a life insurance policy based on contributions made each year. If the tests are met, the life insurance policy maintains its tax-favored status — death benefits paid to beneficiaries are free from income tax, cash value accumulates tax-deferred and withdrawals (and loans) are tax-free.[2]

1 U.S. News & World Report, "Pension vs. 401(k)" December 21, 2018.

2 Under current federal tax rules, you generally may take income tax-free partial withdrawals under a life insurance policy that is not a modified endowment contract (MEC), up to your basis in the contract. Additional amounts are includible in income. The IRS places a limit on how much money can go into life insurance premiums for the policy and how quickly such premiums can be paid in order for the policy to retail all of its tax benefits. If certain limits are exceeded, a MEC results. MEC policyholders may be subject to taxes on distributions on an income-first basis, that is, to the extent there is gain in their policies and penalties on any taxable amount if they are not age 59½ or older. Loans taken will be free of current income tax as long as the policy remains in effect until the insured's death, does not lapse and is not a MEC. Please note that outstanding loans accrue interest. Income tax-free treatment also assumes the loan will eventually be satisfied from income tax-free death benefit proceeds. Loans and withdrawals reduce the policy's cash value and death benefit, may cause certain policy benefits or riders to become unavailable and may increase the chance the policy may lapse. If the policy lapses, is surrendered or becomes a MEC, the loan balance at such time would generally be viewed as distributed and taxable under the general rules for distribution of policy cash values. In addition, withdrawals, policy loans and any accrued loan interest may cause your policy to lapse even if you are in a period of coverage under the No-Lapse Guarantee Rider. Speak to your financial professional before taking any withdrawals or policy loans.

What a properly funded 7702 cash value life insurance policy can do for you

When properly designed, a 7702 life insurance policy with cash value can make the other assets in your three buckets more efficient. That's because it provides:

- A tax-free benefit for beneficiaries. The death benefit can help survivors by self-completing retirement funding if the main income earner passes away.
- Tax-free withdrawals and loans from the policy's cash value to fund your retirement income.
- Tax-deferred, compounded accumulation, similar to IRAs and 401(k)s.
- Flexibility to delay withdrawals past age 70½.
- A way to reposition and further diversify assets.
- The opportunity to use the cash value for qualifying long-term care expenses, if a long-term care rider is in place. The Long-Term Care Services℠ Rider has an additional cost, restrictions and limitations. A client may qualify for the life insurance, but not the rider. The rider is paid as an acceleration of the death benefit.

Things to think about before moving ahead

- If you do not keep paying the premium on a life insurance policy, you will lose substantial money in the early years since a life insurance policy generally takes years to build up substantial cash value.
- To be most effective, you need to keep your policy until death.
- You must qualify both medically and financially for life insurance.
- Generally, there are additional charges associated with a life insurance policy, including, but not limited to, a front-end load, a cost of insurance charge, potential surrender charges, additional benefit rider costs and administrative charges.

Turn to us for your life insurance

With careful planning, our portfolio of permanent life insurance products can be a key component of a well-balanced, tax-efficient retirement portfolio. That's because our life insurance offers:

- Competitive, potential cash value product options.
- Conservatively priced products designed for cash value accumulation, in addition to life insurance protection.
- Illustrations that show how our products can help supplement retirement income.
- A wide selection of riders to choose from, including the Charitable Legacy Rider®, which offers an additional death benefit to the charity of your choice at no added cost.

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