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Life insurance to diversify from concentrated asset protection

A hallmark of wise planning is to diversify risk across a range of assets and asset types. Because any one asset or asset class might underperform in a given year, diversification into other assets can offset that underperformance. This risk can be magnified where clients have a heavy concentration in one stock or asset. Now, capital gain rates are at near-historic lows and the stock market is in a position of strength, may be a time to consider repositioning. Where a client has a life insurance need, a life insurance death benefit might also help add stability to a client's overall wealth transfer plan.

The Henrys have 25% of their net worth in Acme, Inc.

Mary and John Henry are 55 years old and on track with their retirement savings. They are high earners, but not rich yet. John knows he needs to provide for Mary and their family should something happen to him. They have a net worth of $2,000,000 exclusive of their home and college funds. Six years ago, they bought stock in a medical tech company, Acme, which has skyrocketed to $500,000. They lost a considerable amount of their net worth (and the stock's value) in the 2008 market collapse. Now it has substantially recovered, capital gain rates are low and they are exploring options.

A life insurance strategy

Their financial professional shows them an approach where life insurance might be able to provide multiple solutions. Selling a portion of their stock in Acme will help reduce their exposure to a single large position; and by selling now, they can take advantage of the historically lower capital gain rates. Moving a portion of that gain into life insurance can help the Henrys:

- **Provide a needed death benefit for their family.**
- **Provide a tax-deferred source of cash value accumulation and a limited source of supplemental funds for their retirement.[1]**

- **Provide a specified sum to their family for wealth transfer, regardless of the volatility of their other assets. A sale today can capture gains at low capital gain rates.**

- **If they elect Equitable's Long-Term Care Services℠ Rider, John may have a source of funds should he become impaired, but that will erode the death benefit, which will hurt this strategy. In some cases, a separate long-term care strategy may be better.**

The ideal client

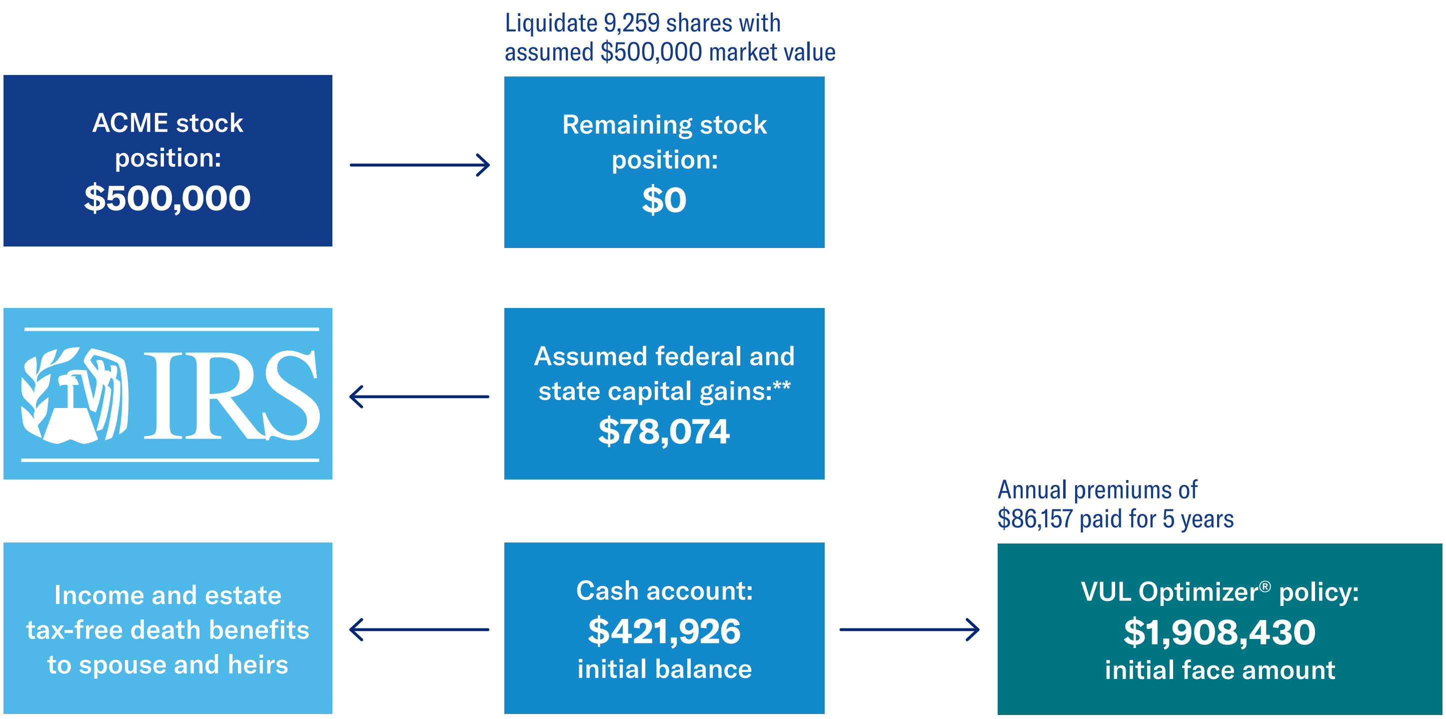
- Has a life insurance need
- Is 45–65, but might be older
- Has a net worth even as low as $1,000,000 exclusive of residence
- May be a corporate executive with salary and benefits tied to a company that also makes up a large portion of their net worth
- May have a large portion of wealth tied to a stock with family or sentimental value

Other considerations for the Henrys

- They will have limited access to the funds. With the stock, they can access cash more readily.
- They have the potential for lost asset appreciation if they live beyond a crossover point. This is the point where the value of their portfolio could exceed the amount of the life insurance death benefit.
- They face accelerating taxes in the form of a capital gains tax when they sell all or a portion of their concentrated portfolio.
- In order for this concept to work properly, they must hold the life insurance until death. Also, additional premiums may be required, depending on the performance of the policy, including premium payments until death.

How this works for the Henrys

In this approach, John or Mary may sell some or all of their stock in Acme, locking in their gain and during a year with low capital gain rates. Here they sold everything, but it doesn't need to be an all-or-nothing strategy. The couple carves out an amount for capital gain taxes and uses the balance for life insurance premiums.* The flow of the transaction and the numbers look as follows.



* Life insurance policy based on a 55-year-old male with an underwriting category of standard plus, non-tobacco. The initial death benefit is $1,908,430 (Option A) in a VUL Optimizer® policy, $86,157 premiums for 5 years, assuming a 6% net crediting rate on the policy and 1.5% crediting on escrowed cash from the sale of the stock before it is applied to premiums. Assuming guaranteed values, the policy will lapse at age 75.

** Includes 3.8% Medicare surcharge tax.

What have the Henrys accomplished

John and Mary sold their stock when it was trading at $54.[2] The chart below shows how much Acme would need to have appreciated each year to match the benefit the family might see from life insurance. Now the family has locked in both gain in the stock and purchased a death benefit with the funds. Using VUL Optimizer® might produce potentially higher death benefits or cash values. The numbers below are even more dramatic if the life insurance is held in an irrevocable life insurance trust.

Age	Death benefit plus net cash from sale	Share price equivalent	Required rate of return on stock to match	Share price equivalent — insurance in ILIT	Required rate of return on stock to match
56	$2,247,725	$242.75	349.54%	$380.16	604%
65	$1,908,431	$206.11	14.33%	$343.52	20.32%
75	$1,908,431	$206.11	6.93%	$343.52	9.69%
84 (LE)	$1,908,431	$206.11	4.73%	$343.52	6.59%
95	$1,908,431	$206.11	3.41%	$343.52	4.73%

At John's life expectancy (age 84), Acme would need to have increased to $206.11 to match the benefit John's beneficiaries would receive had he not captured his gain and redeployed his funds into life insurance. The results are even more dramatic if the life insurance were held in an irrevocable trust. There, at age 84, the stock would need to have increased to $343.52, or 6.59% average annual growth, to match the death benefit available to John's beneficiaries.

For more information, please call Equitable Advanced Markets at (860) 409-1290.

1 Loans taken will be free of current income tax as long as the policy remains inforce until the insured's death, does not lapse or mature, and is not a Modified Endowment Contract. This assumes any loan balance will eventually be repaid with income tax-free death benefits. Loans and partial withdrawals reduce the policy's death benefit, which will hurt the strategy and increase the chances a policy may lapse.

2 This assumes Acme, Inc. is sold when it is trading at $54. Long-term capital gain is calculated using a basis of $20. The insureds' annual income is assumed to be $260,000, and their capital gains are taxed at a rate of 15%.

Neither Equitable nor its representatives offer tax or legal advice. This presentation, in oral or written form, should not be constructed as such. This is not intended to replace business insurance needs analysis. If you elect to implement a program funded with life insurance, please be aware that there are many forms of life insurance and you should work with your professional advisors, including a licensed life insurance representative, to determine the most appropriate form of life insurance for your business needs.

All guarantees are based on the claims-paying ability of the issuing company, either Equitable Financial or Equitable America.

The hypothetical illustration is a supplemental illustration and must be read in conjunction with the basic illustration. The basic illustration contains values using the same underwriting assumptions as this supplemental at both guaranteed charges and guaranteed interest rates, and contains other important information. The values represented here are for a $1,908,430 VUL Optimizer® policy on a 55-year-old male standard plus non-smoker. The values reflect the cost of 5 years of premiums. The values represented here are non-guaranteed and assume current charges and a current interest rate of 6.42%. If guaranteed rates and charges are used, the policy would fail in year 24.

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