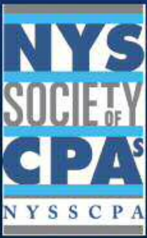
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Questions Regarding Client's Life Insurance Policies That Need to be Asked

If you or your client purchased a permanent Life Insurance policy from the mid 80s through 2003, there's an 80% chance that the type of life insurance purchased was a Flexible Premium Life Insurance contract that, unlike their more expensive predecessor, Whole Life Insurance was **not guaranteed** to last for the rest of one's life. As a result, approximately 23% of those **non-guaranteed** contracts are now expiring prematurely.

HOW CAN THAT POSSIBLY HAVE HAPPENED?

In the mid 80s when interest rates were in the 17-18% range, many insureds withdrew their accumulated cash values from their life insurance contracts, earning 3% and transferred them into higher-yielding bank accounts and CDs. In order to stop this tremendous outflow of funds from the cash value accounts of life insurance policies to the banks, the insurance industry (E.F. Hutton, 1982) developed a new product known as "Flexible Premium life Insurance." The most common type was called "Universal Life Insurance." While it paid a competitive interest rate, that rate was not guaranteed and that fact was not clearly understood by the private owners and trustees when it was purchased.

HOW DID SUBSEQUENT RATES AFFECT THE PERFORMANCE OF POLICIES?

Since interest rates were substantially higher when these contracts were first taken out in the mid 1980s, individuals incorrectly assumed that their contracts would continue to earn these higher interest rates each and every year. However, as rates subsequently decreased over the years, the original premiums were unfortunately not adjusted upwards in order to make up for the resulting reduced rates and reduced earnings.

The sons and daughters acting as amateur trustees weren't aware that their life insurance should have been treated as a "Buy and Manage" asset just like any of their other stock and bond or real estate investment portfolios, instead of as a "Buy and Hold" asset that they forgot about. This neglect, in addition to the reduced earnings, has adversely impacted the performance and duration of their life insurance policy's coverage.

ISN'T THE INSURANCE COMPANY/AGENT/BROKER MONITORING THE SITUATION SUPPOSED TO PREVENT THIS FROM OCCURRING?

No, the insurance company is required to merely send out an annual statement containing all of the required information, which it does. The agent is contracted with the insurance company, and solely responsible to distribute the insurance policy to the trustee/owner. It's the trustee/owner's responsibility to manage the contract and pay a sufficient premium in order to keep the contract in force. As a matter of fact, the insurance company stands to profit greatly when an insured, after years of paying their premiums, decides to drop their coverage as all the past premiums paid are 100% profit to the insurance company, since they will never have to pay out a death benefit claim.

HOW CAN THIS HAPPEN SINCE I PAID MY PREMIUM IN FULL AND ON TIME?

Paying the scheduled premium was not enough. In a declining interest rate environment, the responsibility to pay an adequate premium to keep coverage in force for the balance of an insured's lifetime on a non-guaranteed contract was

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transferred to the trustee. Problem is that neither the private owner, nor the trustee, nor their advisers realized that they assumed 100% performance risk and the responsibility to manage their contract.

WHAT OPTIONS ARE AVAILABLE TO TRUSTEES TO AVOID FUTURE LITIGATION?

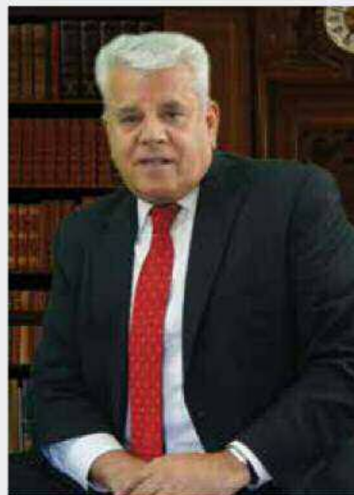
Five options to prevent a dispute within family members or with their adviser:

1. They can either pay a higher premium to keep the same coverage in force while extending the guarantee period. The longer the guarantee period, the higher the cost.
2. They can reduce the death benefit in order to extend the guarantee period, while still maintaining the same premium.
3. They may, depending on the insured's health, be able to purchase a new life insurance contract at the same premium with better benefits and still extend the guarantee period.
4. They may be able to sell the life insurance contract, known as a "life settlement," where they may receive more money than the cash value offered by the insurance company.
5. A combination of the four available options listed above.

LEARN MORE ABOUT A LIFE INSURANCE POLICY PERFORMANCE EVALUATION

To learn and determine whether it has affected your or a client's life coverage, or your relationship as a professional trustee, you can view several articles on the website below. You can also suggest that a client arrange for an independent fee-based life insurance policy performance evaluation and life expectancy report to maximize and protect a client's best interest. The sooner it's done, the more options will be available to fix the problem.

Doing so will not only make certain that your or your client's legacy plans are fulfilled by having their family or charity receive the tax-free dollars originally intended, but it can also provide attractive living benefits for the insured today. Benefits that weren't available at the time the original policy was purchased. For example, up to $120,000 of qualifying costs for long-term care, annually adjusted for inflation, can (as of January 2011) be withdrawn tax-free from the death benefit of a life insurance policy with an LTC/CC rider.



BY HENRY MONTAG, CFP, CLTC

Henry Montag CFP, CLTC, in practice since 1976, is a Principal of the TOLI Center East & provides CPE & CLE credits to organizations such as the NYS Bar Association, Nassau and Suffolk State Society of CPAs, NcCPAp, and the AICPA. His articles on trust-owned life insurance have appeared in publications such as the New York State Society of CPAs, the *Tax Stringer*, *Tax Facts* as well as the NYS Bar Association's *Senior Lawyer* and the *Elder Law Journal*. He has authored a book for the A.B.A on life Insurance performance evaluations which will be released Fall 2015. He's been a source for *The Wall Street Journal, Investor's Business Daily*, *Newsday*, *Long Island Business News* and has appeared as a guest on Fox News and News 12.

henry@thetolicentereast.com
www.thetolicentereast.com
516 695-4662