

AT Think OBBBA and the repurposing of life insurance portfolios

By [Henry Montag](#) October 20, 2025, 3:41 p.m. EDT9 Min Read

One of the most significant features of the One Big Beautiful Bill Act that Congress passed in July is it permanently eliminated the federal estate tax liabilities for individuals with less than \$15 million of assets in their estates, or \$30 million for married couples.

This brings up an important choice for many ultra-high-net-worth individuals who previously had to allocate up to 40-45% of their assets to pay their share of their federal estate tax liability, which for the most part was due nine months after an individual's death. The vast majority of those high-net-worth individuals chose to pay for those death taxes using a life insurance policy because it was the most tax efficient, leveraged and economical vehicle available.

The advisor's role, guiding choices

Legal and tax advisors can play a significant role in alerting their UHNW clients to the availability of the various options and strategies regarding what to do with their now unneeded life insurance death benefit. In addition, an advisor should also be aware of the increasing numbers of clients that are continuously being notified by their life insurance company that their non-guaranteed universal life insurance coverage, which was so popular over the last 25+ years, is now expiring years earlier than anticipated. This is occurring as a result of years of reduced interest rates and neglect on the part of the owners who weren't aware they should have increased their premiums over the years when interest rates kept declining.

The question today becomes what to do with those multiple millions of dollars of the client's current death benefit that are no longer needed as a result of the increased estate tax exemptions. Secondly, since more than 45% of those policies were non-guaranteed universal policies, 30-35% of the coverage in those policies is currently expiring prematurely and needs to be dealt with as well.

Advisors to these high-net-worth clients should have an understanding of the available options rather than just assume that if the death benefit is no longer required for estate tax purposes, then the client should just surrender the policy for its cash value. The purpose of this article is to provide you with several other options to re-arrange or re-purpose a client's current life insurance portfolio in the most beneficial manner.

An evaluation should be made as to which policies to keep or alter the premium in some manner to obtain additional benefits, or in some cases end the coverage. It's imperative not to allow a policy to lapse prior to the insured's death if there are any gains in the policy, because a lapse in coverage would trigger a phantom income tax on those gains, as well as any outstanding loans.

Options worth considering

Any of the options listed below is effective for a \$250,000 policy, a \$2.5 million policy or a \$25 million policy. These same options are available for a trust-owned life insurance policy as well as for an individually owned life insurance policy.

A client can simply maintain their existing coverage to make a charitable donation to a hospital or university for tax purposes or for assets allocated to the next generation in a generation skipping/dynasty trust for grandkids who certainly may have significant estate tax problems of their own one day.

Due to the passage of the Pension Protection Act, an individual can now transfer the cash value of a life insurance policy on a tax-free basis to a "linked benefit policy," which in addition to offering a death benefit, also offers an individual the ability to withdraw dollars from the death benefit of their life insurance policy tax-free, to pay for qualified long-term care benefits where one dollar can become four to five dollars.

People are now living longer as a result of modern pharmacology and have accordingly influenced the life insurance industry to financially reward individuals for living healthier lifestyles. Many of today's life insurance policies contain provisions and policies that were not available 20+ years ago. One such life insurance policy is called Private Placement Life Insurance.

The advantage of a PPLI type of a product is that it rewards the purchasers of such multimillion-dollar death benefit policies with institutional products that contain lower costs and fees, fewer restrictions on withdrawals, and are managed by hedge funds rather than mutual funds. This type of specialized product often results in better returns with significantly lower costs than traditional retail life insurance policies that are typically offered to the general public.

Another strategy could be to reduce the death benefit by 15-20% using any of the means described below. They can then increase the premiums up to the modified endowment limits and use the policy for its ability to accumulate cash value on a tax-deferred basis with the intent to later withdraw the cash value on a tax-free basis through a series of surrenders and loans against the death benefit that will never have to be paid back as long as the policy survives the Insured.

This opportunity to supplement one's retirement with tax-deferred dollars, otherwise known as a private pension, was recently made even more attractive as a result of the passage of the Consolidated Appropriations Act of 2021 (Section 7702), which reduced the actuarial interest rate assumptions used by the life insurance companies to define a life insurance contract. Doing so made it possible for the owner of a life insurance policy to place an even larger premium into the policy's cash value without negatively affecting the policies' ability to continue to shelter the growth and distribution of the cash value on a tax-free basis.

Surrender the policy for its cash value

The great majority of individuals who decide to cancel their policies in exchange for the remaining cash surrender value can merely contact their agent or broker (or the company directly) and request a form which, once it's signed, notarized and returned, will conveniently serve to surrender the policy

back to the insurance company that issued it in exchange for the stated cash surrender value.

Policies are often surrendered to the insurance company for several reasons: Customers perhaps no longer need or can afford the increased cost of the coverage. They may want to use the existing cash surrender value to supplement their own retirement income, or they want to make a gift to their heirs while they are alive to enjoy it. Life insurance companies are happy to accommodate both goals as they profit nicely when a policy is surrendered back to the insurer as they get to keep all the premiums and never have to pay out a death benefit. There are better ways for the client to accomplish both of those goals.

An alternate exit strategy

An individual is entitled to sell their life insurance policy as they would their car, boat or home. The U.S. Supreme Court case of *Grigsby v. Russell* (1911), established a life insurance policy as "private property," placing the ownership rights on the same legal footing as an investment property such as stocks and bonds. As such, a life insurance policy can be transferred in whole or part to another person at the discretion of the policy owner. The life settlement market, primarily funded by hedge funds and often referred to as the institutional or secondary market, has greatly enhanced the consumer value of a life insurance policy, often by two to three times the cash value offered by the insurance company, according to a London Business School study.

However, the majority of clients, and many of their advisors, are not familiar with the concept of a life settlement, nor do they feel comfortable about another person owning a life insurance policy on their lives, and in my opinion, rightfully so. The only buyer one should deal with is an institutional buyer.

While a life settlement can be entered into by anyone who owns a life insurance policy, only those policies that have a face value of at least \$100,000, preferably \$250,000, with an insured who is at least 65 years old will be of interest to most institutional investors. Contrary to popular belief, even a healthy individual can receive an offer on a term policy, if the policy is still within the convertible period. However, the more severe the health conditions, the more likely they are to receive a higher offer.

One of the smartest pieces of advice an advisor can give their client is to remind them that if they are in their 60s to 70s and they have a term life insurance policy that's no longer needed or wanted, rather than let it lapse with no value, the owner should attempt to sell the policy as they may be very pleasantly surprised to learn they could turn the unneeded term life policy with no value into a cash offer as long as the policy is still in its convertibility period usually between ages 65 to 75.

Taxation of life settlement

A life settlement on a universal life insurance policy is a taxable event, and the proceeds are taxed in three tiers.

- Tier 1: Tax-free return of cost basis: A portion of the sale proceeds up to the amount of the cost basis or amount paid in premiums is tax free.
- Tier 2: Ordinary income: A portion of the sale proceeds above the cost basis and up to the policy's surrender value is taxed as ordinary income.
- Tier 3: Long-term capital gain: Any remaining sale proceeds above the surrender value are only taxed as long-term capital gains.

Life settlement taxation case example

- Policy type: \$1 million universal life
- Premiums: \$70,000 (cost basis)
- Cash value: \$80,000 (surrender value)
- Policy sale price: \$300,000 (settlement amount paid to policy owner)
- Tax-free return of cost basis: \$70,000 (cost basis or amount paid in premiums)
- Ordinary income: \$10,000 (portion of sale proceeds above cost basis (\$70,000) and up to surrender value (\$80,000))
- Long-term capital gains: \$220,000 (remaining sale proceeds (\$300,000 less \$70,000 less \$10,000))

Ever since the creation of the first non-guaranteed life insurance policy known as universal life insurance came into being in 1982, life insurance policies have required active management to continue to operate as the owner hoped they would. However, as a result of sustained reduced interest rates and neglect over the last 25+ years, 35-40% of those policies are now expiring prematurely.

Today more than ever, UHNW clients face a choice of what to do with their unneeded life Insurance policies, while many other clients are in the process of discovering that their non-guaranteed universal policies are expiring earlier than anticipated, and the ability to sell a policy to an institutional investor can make the difference between receiving cash or a tax bill.

While there are many options and strategies to consider before a decision is made, many clients will just take the easiest way out by simply surrendering their policy back to the insurance company. In so doing the insured will inadvertently be giving up valuable benefits they are contractually entitled to as well as opportunities and cash assets.

The most important decision in considering a settlement option is selecting an independent, experienced licensed life settlement broker, a professional who will provide guidance and assistance while contractually affirming their fiduciary duty to the seller and assist the accountant, their client and their trustee in obtaining the best possible offer, one who has access to and understands the marketplace and is adept with the negotiating process necessary to represent the client's best interest.

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