Life Insurance Planning Strategies

Life Insurance in Retirement Planning

PRODUCER GUIDE

Help your clients supplement their retirement income (tax-free retirement distributions), while protecting their loved ones' financial security (death benefit) and providing tax-deferred growth (cash value accumulation).

The unique characteristics and tax advantages of life insurance can help protect the financial security of families during their working years and provide tax-free distributions during retirement.

An indexed universal life (IUL) policy offers the flexibility of a traditional universal life insurance policy with a death benefit, with the potential for significant cash value accumulation using higher credited interest rates and downside protection with a minimum guaranteed interest rate.

An overfunded IUL can provide supplemental tax-free retirement income, can bolster asset diversification — a fundamental part of any sound financial strategy — and enhance tax diversification.

What is Life Insurance in Retirement Planning?

Life Insurance in Retirement Planning (LIRP) is a strategy that deliberately overfunds a life insurance policy — without violating the modified endowment contract (MEC) rules — to build sufficient cash value to allow tax-advantaged withdrawals of basis first and then policy loans to provide a supplemental source of funds during retirement.

The "Why" — Tax Diversification

When it comes to managing client risk in saving for retirement, tax diversification can be as important as asset diversification.

Clients own a variety of investable assets and — excluding their primary residence — we can break those asset classes down by tax status. Typically, some of the largest types of assets owned by a client are tax-deferred and, often, pre-tax qualified accounts, such as IRAs and qualified retirement plans (QRPs), or nonqualified annuities. These can be referred to as tax-me-later investments.

Stocks, bonds, mutual funds, real property and closely held business interests are generally considered to be currently taxable assets, producing dividends, interest, long- and short-term capital gains, rents, etc. We can refer to these investments as tax-me-now assets. The final segment is typically the least represented: nontaxable and tax-advantaged. These are tax-me-never and generally include Roth IRAs, municipal bonds and life insurance.

Tax Diversification

TAX-ME-NOW INVESTMENTS	TAX-ME-LATER INVESTMENTS	TAX-ME-NEVER INVESTMENTS
Stocks	IRAs	Roth Accounts
Bonds	QRPs	Municipal Bonds
Mutual Funds	Nonqualified Annuities	Life Insurance

Combine an investment portfolio heavily invested in tax-me-later investments with the possibility of higher — not lower — tax rates in retirement and clients are faced with the risk of reduced income in retirement.

Tax-Me-Never Investments

Roth IRAs are a popular tax-me-never investment option. The widely touted tax advantages include tax-deferred accumulation and potentially tax-free distributions, no required minimum distributions (RMDs) and an income-tax-free inheritance for beneficiaries. Unfortunately, Roth IRAs are not available for certain high-income earners and the amount that can be contributed annually to a Roth IRA is fairly limited.

While not a substitute for a qualified account, an overfunded IUL policy may provide the client with valuable benefits. The cash value of an IUL policy grows tax-deferred and the death benefit is generally received by beneficiaries tax free. And, of course, there is no requirement to take mandatory distributions beginning at any age.

Additionally, high-income earners who have contributed the maximum to their tax-me-later qualified plans and IRAs can still contribute to an IUL policy. There is also no limit on the amount of money that can be contributed to the IUL policy as long as the MEC rules are not exceeded, and there is sufficient insurability.

The "How"

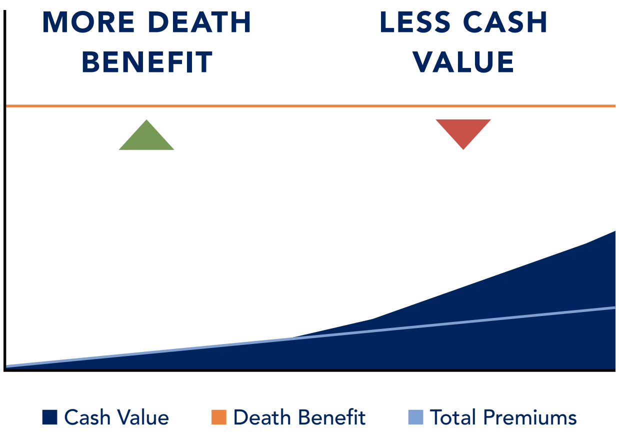
Designing an overfunded IUL policy requires a shift in conventional thinking. When it comes to purchasing life insurance, most clients seek to obtain the highest death amount for the least amount of premium. The result is an increased net amount at risk and, with universal and variable life insurance policies, an increased cost of insurance (COI). The increased COI reduces the amount available for tax-deferred growth.

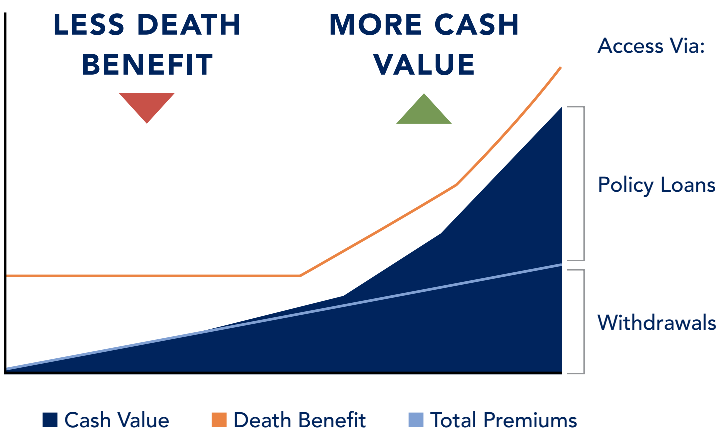
If, on the other hand, COI is controlled and minimized, what happens to the cash value? There is more cash remaining for tax-deferred growth.

By designing a policy with a minimum, non-MEC death benefit, we reduce COI, allowing more of the premium to be applied to cash value accumulation.

When the client wants to access cash in the policy for retirement, the client can withdraw his basis in the IUL policy tax free. Withdrawals from a non-MEC life insurance policy are taxed on a "first-in, first-out" (FIFO) basis, also known as the "cost recovery rule." Thus, withdrawals are included in gross income only to the extent they exceed the client's basis or investment in the contract (as reduced by any prior excludable distributions under the contract). After all the basis has been withdrawn, the client can take a loan out against the policy's cash value. Policy loans are not currently taxable as they are not treated as distributions.

Withdrawals and policy loans will affect the death benefit payable under the policy. Policy loans should be closely monitored to protect against accidental lapse of the policy and potential tax liability.





It should be emphasized that a LIRP strategy can work with a maximum funded policy. The strategy's potential may be negatively impacted with reduced funding. Sufficient premium and account value are necessary to cover insurance costs and prevent lapse. Index returns are not guaranteed and do not ensure that the policy will stay in force.

The graphs shown are hypothetical for illustrative and educational purposes only to describe the impact of possible premium and death benefit designs on cash value potential. They do not represent the cost or performance of any specific life insurance product.

Unique Characteristics and Tax Benefits of Life Insurance

Income Tax-Free Death Proceeds

As long as a permanent life insurance policy is in force, it will provide a death benefit, regardless of whether the insured dies within the first thirty days or thirty years later.

Tax-Deferred Buildup of Cash Values

Premiums paid into a permanent life insurance policy are used to pay the basic insurance policy costs and, if paid in sufficient amount, will accumulate equity or cash value in the policy. This cash value grows tax deferred.

Tax-Free and Tax-Advantaged Distributions of Cash Values

Withdrawals of cash value up to cost basis are received free of income tax. Policy loans are not included in income at the time of the loan.[1]

The "Who"

A LIRP may be an appropriate strategy for the following clients looking for supplemental retirement income:

- **35 to 65 years old:** LIRP is a long-term strategy requiring long-term commitment and full funding.
- **High-income earner:** Able to predictably commit additional funds to a non-qualified investment annually.
- **Already contributing the maximum to qualified retirement plans and IRAs:** Taking full advantage of immediate tax savings and building tax-me-later investments.
- **Insurable:** Must be able to meet medical and financial underwriting requirements.

MODIFIED ENDOWMENT CONTRACTS

The tax advantages afforded a life insurance contract are conditioned on the policy meeting strict requirements outlined in the tax code. To deter a life insurance policy from being more investment-oriented than death benefit-oriented, the tax code began classifying life insurance contracts that failed to meet tests designed to establish permissible funding levels in relationship to the policy's death benefit as Modified Endowment Contracts (MECs). While the cash value of a MEC continues to grow tax-deferred and its death benefit remains income-tax-free, lifetime distributions are taxed as income first and a recovery of basis second. Thus, withdrawals and policy loans from a MEC are taxable as income to the extent that the cash value of the contract immediately before the payment exceeds the client's basis in the contract.

1 Loans will accrue interest. Loans and withdrawals may generate an income tax liability, reduce the account value and the death benefit, and may cause the policy to lapse. Sufficient premium and account value are necessary to cover insurance costs. Index returns are not guaranteed and do not guarantee that the policy will stay in force.

Frequently Asked Questions (FAQs)

Are there any disadvantages to using the LIRP strategy?

While an IUL policy allows premium flexibility, a successful LIRP strategy requires that the client be able to commit to making significant premium payments for several years and avoid taking distributions for several more years to allow for tax-deferred growth.

It is important to remember that the underlying vehicle is a life insurance policy. The client has to be insurable. Surrender charges will apply in the early years. If a life insurance policy with an outstanding loan balance lapses, the amount of the loan balance will be included as income to the extent there is gain in the contract.

Are the premiums deductible?

In general, premiums paid for life insurance are not deductible. However, when properly designed, the cash value accumulates tax-deferred, distributions may be income tax-advantaged, and death benefits are generally received income-tax free.

Why is Columbus Life's Indexed Explorer *Plus*® potentially a good vehicle for a LIRP?

Indexed Explorer *Plus*® could be an excellent vehicle for the LIRP strategy, offering enhanced growth potential with competitive current interest crediting rates, its Overloan Protection Rider, and possible zero-net-cost loans or Participating Rate Loans.

- Indexed Explorer *Plus*® offers a choice of four account options.
- The Overloan Protection Rider will prevent a policy from lapsing due to excessive loans and preventing a taxable event for your client.
- The Standard Loan Option[2] offers a guaranteed maximum 0.50% net loan spread in all policy years. On a current basis, zero net cost loans are available in years 11+.
- The Participating Index Loan Option[2] offers a guaranteed maximum loan interest charge of 6%; however, a lesser interest charge may be declared by the company (state variations may apply).

Why Columbus Life?

With heritage dating back to 1906, Columbus Life provides retirement, estate planning and advanced business planning services to the affluent market through a nationwide network of independent producers and registered representatives. When you consider financial services and products, the resources and expertise of the provider are paramount. We are a leader in financial security, service quality and performance excellence — a top-rated company providing life insurance and annuity products for clients in the District of Columbia and all states except New York. We are part of Western & Southern Financial Group, a family of financial services companies whose heritage dates back to 1888 and whose assets owned ($45.4 billion) and managed ($23.1 billion) total $68.5 billion as of Sept. 30, 2016. In addition, we differentiate ourselves as a company of choice through our high ratings for financial strength from leading industry rating sources. Find out more about our financial strength and distinguished history at **www.ColumbusLife.com.**

2 Once a Standard Loan is selected, a Participating Indexed Loan may not be chosen or be outstanding.

IUL is a universal life policy. It has insurance related costs. Premiums paid must produce sufficient cash value to pay insurance charges. Indexed returns do not protect against lapse if premiums and returns do not provide sufficient cash value to cover loan interest and insurance costs. Your clients must understand that loan risk means loans may well not be zero cost. Such loan risk and interest costs will reduce account value and will contribute to a risk of policy lapse if account value becomes insufficient to cover charges.

Product issued by Columbus Life Insurance Company, Cincinnati, Ohio. Columbus Life is licensed in DC and all states except NY. Indexed Explorer Plus Flexible Premium Universal Life Insurance Policy series CL 88 0707, Overloan Protection Rider series CLR-178 0707.

Payment of benefits under the life insurance policy is the obligation of, and is guaranteed by Columbus Life. Guarantees are based on the claims-paying ability of Columbus Life. Products are backed by the full financial strength of Columbus Life.

Earnings and pre-tax payments are subject to ordinary income tax at withdrawal. Withdrawals may be subject to charges. Neither Columbus Life, nor its agents, offer tax advice. For specific tax information, consult your attorney or tax advisor. Interest rates are declared by the insurance company at annual effective rates, taking into account daily compounding of interest. Product and feature availability, as well as benefit provisions, vary by state.

Life insurance products are not bank products, are not a deposit, are not insured by the FDIC, nor any other federal entity, have no bank guarantee, and may lose value.

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