

The Large Case Design

Memorandum

Private Financing

As many a politician and CEO have said, 'it's a shame to waste a good crisis'. Taking advantage of opportunities to profit while the economy is down is the mark of an astute investor. It won't be long before economic recovery regains momentum and opportunities to transfer assets at steeply discounted valuations or pegging loans to the current incredibly low AFR disappear. Clients with a modicum of foresight and any reasonable time horizon should be looking for ways to reorganize their taxable estates. Considering the towering mountain of debt the government has created I think it's safe to assume that: the estate tax is not going away, interest rates will rise and inflation will be a problem for years to come. Add to that the fact that real estate (commercial and residential) and other tangible assets are at decade's low valuations, and you have to conclude that this is a potentially once in a lifetime opportunity to do aggressive estate planning. Opportunities of this magnitude will not present themselves for long and in the case of many older clients maybe never again.

Even though your clients feel less wealthy than they did a couple of years ago this may be the perfect time to discuss asset transfer strategies with them. Two relatively straightforward ways of transferring wealth to the next generation utilizing life insurance are particularly attractive right now: Private financing and gifts of depreciated assets.

Private financing makes sense because a lump sum loan can be made to an ILIT utilizing the long term AFR (currently 4.44% for loans originating in Feb 2010) or in the case of a stream of loans the mid-term rate (currently 2.82% for loans up to 9 years originating in Feb 2010). Clients can lend their trusts cash or cash equivalents and have the trust invest the assets for income and or growth. The trust can use the income or appreciation to fund the cost of life insurance premiums without the economic drag of gift taxes. The loan must be repayable to the estate at the applicable AFR and it's best to have the trust pay interest annually to the grantor. Alternately, the trust can repay the entire loan plus interest at the client/insured's death. Either way, using a return of premium rider or other face amount enhancing method will keep the bulk of the assets in the trust (and out the estate) while still generating sufficient funds to repay the loan.

If your clients have underappreciated assets now is a great time to gift them to an Irrevocable Life Insurance Trust. Assets such as income producing real estate may be valued at a steep discount for gift tax purposes and yet provide enough cash flow inside the trust to pay insurance premiums. If the asset appreciates substantially in the future, the gains will be inside the trust and out of the estate. This applies just as well to stocks in companies that are trading at a discount today but may increase substantially in the future.

In addition to the more obvious benefits of these transactions there are also several tax arbitrage opportunities. For instance, there is no tax paid on interest payments made by the trust to the grantor.

Another way to spin this would be to have your client(s) lend their children an income producing asset. Muni bonds would be the best example. Set up the loan at the current AFR and have the children pay for a life insurance policy equal to the corpus with the net income. Because of the disparity between the AFR and the income from the asset there should be plenty left over for insurance. At death the asset reverts to the estate and the children receive the tax free death benefit to be used to pay estate taxes. This could be an excellent solution where the estate's other assets are difficult to monetize such as real estate or art.

There are many creative ways to utilize private financing or asset sales that can result in a substantial purchase of life insurance. We've used these methods successfully for years, but the environment for this type of planning has never been better. It's a shame to waste an economic crisis. Let us show you how your clients can benefit from some great time sensitive opportunities.

- Ron Sussman, CEO

The opinions expressed in this memorandum are those of the author and are intended to provoke discussion and positive change within the industry.

At CPI Companies we understand the complexities and demanding nature of the large case life market. Allow us to assist you with your next important case.

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