

The Top 22 Overlooked Uses of Life Insurance in 2013

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My goal today is to give each of you at least four or five practical sales, marketing, and closing techniques that you can start implementing right away and promise you that from these techniques you can generate at least another \$50,000 a year or more of revenue. Would that be all right with you? Okay!

Now, of the most commonly thought of, or standard uses, for life insurance, the first one is income replacement. This is one that many people think about, particularly when you've got a young working couple or someone young who is supporting children, and in case they were to pass away, that will replace their income. Buyout of other business partners, that's a very standard use. And, I know you've all heard about using life insurance to make estate tax payments.

I want to digress on this one for just a few minutes because I am an estate planning attorney and this is one of my favorite topics. It doesn't matter what the exemption is going to be this year or next year. Either way you know there will be an estate tax no matter what. Even if Congress does nothing, we're going to go back to the pre-Bush years where we're going to have a \$1 million exemption with a 55 percent tax. So something is going to give somehow, somewhere, there is going to be a change.

But regardless of the change, don't underestimate the use of life insurance to pay estate taxes. I want you to think about this. Because the estate tax future right now is uncertain, do you think the people who have an estate are even more worried about it? This is a great time actually to sell life insurance for estate taxes even though technically right now the estate tax laws are uncertain.

I want to point out a few items that you may want to look at when selling life insurance for estate tax purposes. You need to first of all take the clients through these steps and show them how their taxable estate is calculated. Most people underestimate the size of their taxable estate because it includes fair market value of all the real estate or business, and you know how people

will tend to underestimate that. It includes, of course, all their investment assets, but a couple of assets that people neglect to think about are all their retirement benefits and the full, matured amount of any life insurance that they own.

Now we'll talk about moving life insurance out of the taxable estate such as using an irrevocable trust a little bit later. When you actually add it up, people are worth more than they think. But it gets even bigger because what is the value that determines estate tax, the value today or the value when someone dies? So if we project out the value, we can show clients that their estate, when it comes time, is probably going to be much larger than today.

This is particularly true because the real estate market is down. So here a lot of people understand that it's pretty likely that even if they do nothing, just the real estate market itself over time will probably increase their estate, not including income they don't spend or good investing. Here you use what's called the Rule of 72. You should know this. If you take 72 and divide it by the assumed rate of annual growth of an asset, it will tell you how long it takes to approximately double in size.

Here is what I say to clients, "From markets rebounding, from income that you save and you don't spend, and from just good investing, do you think it will be conservative to say that between now and the date you die, on average, your estate would go up 6 percent a year from all those factors?" Pretty conservative, right? We take 72, divide it by 6, and what it tells us is that roughly every 12 years that estate will go up. So this person now has a \$2 million estate. They're thinking it's not taxable, the exemption may wind up at \$3 million or \$5 million. But now you show them, well, wait a minute, actually if you leave 12 years you or your spouse, it goes to 4 and another 12 years, it goes to \$8 million. That's the estate size that's going to determine the estate tax.

The failure to project future value winds up in a lot of under sale or non-sales of life insurance. The second factor is the exemption. Here I would typically do is say the worst case scenario is going to be \$1 million and probably the best case is about \$3.5 million. So now we'll compute it based on those two applying a tax rate of typically 50 percent. Why do I say 50 percent? Well, it

could wind up at 45 percent and it could wind up at 55 percent, but 50 is an easy number for people to understand and it's a good average.

So we've shown them this is what your real tax issue is going to be. It's important to discuss at this point why it's so impactful, so negative a consequence for their family to have to pay tax because you know a lot of people will say, "Well, my kids are going to get more than they deserve anyway, right?" or "Who cares if they have an extra tax?" But what often happens is that much of the assets clients own is illiquid. It's value in their home, it may be in their business, it may be in other assets that, although they could be liquidated such as stocks or mutual funds, how do they know whether they're going to die in an up or down market?

The reality is that in order to come up with cash—and this is a key thing I tell clients—that tax is due in cash nine months after date of death. If you're married, second death typically. The IRS will not accept the stock certificate. They will not accept a deed, it's got to be cash. How many people, when you show them the tax is going to be \$1 million or \$2 million or whatever it is, have that kind of cash? They typically don't. And this can force a fire sale where assets have to be sold in a bad market, or they have to be sold at a discount to quickly move them and come up with the cash. But also, now your family is not going to receive the asset that was sold. What if that was the apartment building or the business you wanted your kids to get?

I want to dwell on a little bit about estate tax because here you can show them the leverage of life insurance versus other investments since we have a knowable amount that will be available at death regardless of the investment, regardless of the investment return. That's the key thing to explain to them. Of course, if set up properly, it can be both income and estate tax free. We're going to talk about that a little later. I don't want you to overlook this common use because I think many of you have the opportunity to sell more insurance for estate tax purposes.

These uses I've covered for life insurance are far less emotionally compelling than the ones I'm going to talk about. I had someone ask me about giving him some tips on how he could approach prospective clients in selling life insurance. One of the things you're going to see is that my approach is the opposite of what most financial advisors, attorneys, and insurance agents use.

They come out with the life insurance immediately and then try to explain how it works. I do the opposite. I look at issues and problems and then I only pull out the life insurance at the end as the solution. That's why over the years I and my law firm have historically generated millions and millions of dollars of commissions in life insurance sale. So I'm going to share with you things that actually work.

When I talk about overlooked uses, the first area of use is estate planning, not involving estate taxes. The giant foot in the door is important because if you can get in by talking about estate planning, you will almost invariably find some use or application for life insurance as well as annuities. This is a great way to start a meeting where they don't look at you as a product sales person. This is something that's really important to be super successful—to get yourself to that next level of production.

The first overlooked use in the estate planning context is what I call estate equalization. There is one big key here. You should be looking at the estate plan. You don't have to be a lawyer to read this gobbledygook of legalese. You should be able to look at the distribution section of a trust and understand pretty quickly who is getting what and how they are getting it. That's not hard. Also, as you'll see a little bit later, I talk about you working closely with an estate planning attorney who can help summarize that for you or maybe even produce a flowchart of the trust or a summary letter to make it easy for you.

Here is why. You want to know what the estate plan is—who is going to get what and when. That is a big step forward in terms of sales because here the first question is balancing specific bequests. What do I mean here? How many of your wealthy clients have rental real estate property? A lot of them, right? Actually I would say, of our wealthy clients in our law practice—we have over 10,000 clients—most of them are wealthy from rental property, some from businesses, some from inheritance, and some from a few other things, such as investing.

And here is the problem. Very often, if you look at the estate plan, it says, "I want Bob to get this property, I want Jane to get this property, I want to Jim to get cash." How do we equalize that in terms of value and in terms of what they're actually going to receive? This is tricky because if

there is a specific bequest of real property in that plan and either A) it has to be sold to pay estate tax or, B) we don't have enough equalizing cash to pay the other people their shares, then we have a problem, don't we? So using life insurance in this context is really a great idea.

Also, where they have a business and they might have a situation where just one child, one beneficiary, is going to take over the business or they want to run the business without the others looking over their shoulder, insurance is a great way to do it. Using it to replace a remainder interest to charity in what's called a charitable remainder trust, or CRT. There are some really tremendous overlooked opportunities with CRTs that we'll talk about.

What happens with the CRT is that there is a return of an income stream to the person who created the CRT or placed the asset in it, but at her or his death, the remainder of that trust goes to charity. Then the question is, how do I equalize what went to charity to my other beneficiaries? This is a great place to use life insurance, but it's also a possible annuity sale too because inside the CRT they may want to invest in an annuity to create the stream of income coming out to pay the premiums.

Here is a key concept that you want to make sure the clients understand when you're talking about replacing or equalizing value to one beneficiary with life insurance. It's key for them to understand they don't have to buy the exact same amount of life insurance as what the other guy is getting. Here is why I'm saying this. Let's say child number one is getting \$2 million of property, and they want to equalize that to child number two. Does that mean they have to get \$2 million of insurance for child number two? Well, we'd like to sell \$2 million, but if you come at them only with the option of \$2 million, kind of a all-or-nothing option, and that's expensive, what's going to happen? Are you going to make the sale? No.

One of the things I show people here is to remember life insurance policies are income tax free. If that other beneficiary sells that property, and if it's appreciated since date of death, she or he is going to have some income tax to pay. The person who gets the insurance has no income tax to pay. Also, the insurance could be held in an irrevocable trust, so there is no estate tax to pay, plus, it's 100 percent liquid cash, which the property is not. So what I'm trying to show the client

is maybe you only need to replace the \$2 million asset with only \$1 million of insurance over here. One of the techniques I'll share with you is not to go all or nothing when you make proposals to people because that's where you'll lose the sale, especially if they go to somebody else who says, "Oh, you could have just gotten this and it would have effectively replaced it."

One of my favorite overlooked uses of life insurance is estate planning—to avoid what I call World War III. What am I talking about here? Where remaindermen have to wait for their inheritance. What do I mean by remaindermen? Well, here is a planning scenario that we're seeing more and more. I've been doing estate planning for over 32 years, and here is an interesting factoid. Even five or ten years ago, maybe one out of five couples that would come in had children from more than one marriage. Now it's more like three out of five because of the divorce rate and remarriage. We get a lot more Brady Bunch families and this is a tremendous dilemma for estate planning.

If you see you've got a client where one or both spouses have children from another marriage, and each wants to protect her or his own kids, this is an area where life insurance is a terrific opportunity, huge. What most estate planning attorneys do, believe it or not, is flat out wrong. It's the worst answer. It's something called a QTIP trust, or qualified terminable interest property trust. Any of you ever heard of that? Now, what is that?

Well, typically it's where you've got this situation of a second marriage. Let's say that I have my own kids, I'm the husband. My estate, or a portion of my estate, is going to go into a QTIP trust where my spouse, if she survives, will have the ability to get the income, may have access to the principal for things that she needs, but when she dies the remainder of that trust will pass back to my kids. Think about this. Think about what a World War III this creates while the remaindermen kids are rooting for the spouse to die. I will tell you I've sold more life insurance because of this one thing than practically anything else, and we're seeing it all the time.

Here is what I do. If I've got a husband and wife in that scenario, I say, "Mrs. Jones, do you know that if Bob dies, you're going to have a trust like this?" What can even be worse is she's not even the trustee of this trust, one of husband's kids is! I say, "Look at this, even if you're the

trustee, do you think those kids of your husband will be rooting for you to die? Do you think they will be questioning every investment you make, every withdrawal you make? They will be a royal pain in the you-know-what, and they will create a living hell, World War III for you. Is that what you would like?”

Note, I haven't yet mentioned life insurance at all. Do you think she wants to know what the other option is right now? And it's obviously a very easy one. The husband could set up a policy—and it could either be a single life or it could be a survivor or joint life policy—that will eventually go to his kids. So now my spouse over here can have that pile of tax-free money unfettered, or she can have it in a trust she controls that goes to her, and his kids don't have an interest in it. This is the term I use, “never the twain shall meet.” She gets hers, they get theirs, and never the twain shall meet. We have peace, we have harmony. People like this. Life insurance to the rescue!

What I'm showing you is if you paint a vivid picture here for that spouse of what that QTIP trust would look like versus having a life insurance option, it's huge. You will make a sale here provided that the numbers work out.

A similar situation is where you've got a marriage and they don't have any children from the prior or current marriage together, but they have different families. So after the survivor dies, I want my half to go to my family members, and my spouse wants hers to go to her family members. We've got the same kind of potential World War III issues while that survivor is living. Sometimes the surviving spouse has what we call a life estate or a right to reside in a property. If she has a life estate or right to reside in the property, do those remaindermen (the husband's family) waiting for it want to really pay to keep it up, or do they want to pay to do improvements on it? Do they want to move her, make her miserable so she moves out of the house and they can get it earlier? Okay, you see what I'm talking now. These are the kinds of things that you look at in the estate plan. Is there a QTIP trust, is there a life estate or a right to reside in the spouse? These are the kinds of things that are triggers for possible insurance application.

Here is another scenario where the beneficiaries will be forced to be in business together. This is where you open up the client's mind to really understand the way things will work. I get families all the time where I ask mom and dad, "Do your kids get along?" What do you think they usually say? Of course.

And then I say, "Have you ever heard the expression, 'When the cat is away, the mice will play'?" When you're not there to hold them down and keep them in line, what happens? Civil war, right?" Here is what I'm trying to point out. The kids are going to share ownership of real estate. Mom and dad own one or two or three pieces of real estate, and the kids will get equal shares. They're going to own it equally together. They're going to be partners together.

Now, you start painting this picture for mom and dad and they start seeing, oh, my gosh, did you know... I say this to clients, "If your three kids inherit one-third share of each of your rental properties, did you know that any one of them, even though they own a minority interest, can force the others to sell?" Lots of people don't understand that under real estate law that's true. You can own a very small percentage of a piece of real estate and force what's called a partition and sale. You can force the others to sell. And it might not happen because this one is not getting along with the brothers and sisters. It might be a spouse who wants to get it in a divorce or who wants cash or doesn't get along with the others and that in-law could be the moving party in this whole thing.

Now, I'm painting the picture, and they're seeing what the dilemma is. This could even happen where they're not directly on title, even where you've set up a family limited partnership or limited liability company because one could be in control and all the others are fighting him. So this co-ownership is a real problem. So here is what I talk. I use these phrases.

You'd like to keep it on the family, wouldn't you?

You don't want those divorcing spouses, or others, to be now forcing the sale of the property, do you?

You want to maintain family harmony.

You can set this up in a way so that one or two of them will get the real estate, and the others will get cash. The one who is capable of managing real estate, who wants to do it, who would be

smart enough to do it, will get the real estate. The other gets cash and never the twain shall meet, okay? This is a great place to look at life insurance to generate the needed cash.

Another common estate planning situation is where the surviving spouse wants to make changes. This is something that's a little technical, so I won't go into a lot of detail. But sometimes in a trust, the surviving spouse has what's called a power of appointment, so she or he can adjust the beneficiaries. When she or he does that, it can create a lot of havoc amongst the beneficiaries who may even contest it later. Well, guess what? If we have life insurance in an irrevocable life insurance trust and in the ILIT we put provisions that say the following: If my kids try to fight over the surviving spouse having changed the estate plan, if they attack my living trust or my will, they're going to lose the life insurance, the million bucks. Do you think that's a powerful disincentive? You see what I'm talking about? So that's another way to use life insurance.

Other uses in estate planning include funding special needs of beneficiaries, assuring there will be an amount there to take care of their health, their support, their maintenance, or their education. Of course, the benefit of life insurance is that we don't have to rely on a certain number of years to grow that fund and to rely on a certain investment return. We know it will be there. Now, I will tell you this is an area that has become of greater importance. Why? There are so many more diagnosed diseases and conditions today than there used to be. Isn't that true? I mean, every kid who can't pay attention in school has ADD. More children are diagnosed on the autistic spectrum.

There are so many different types of infirmities now that can also have the opportunity to extend people's lives. People with MS, with other issues like Down syndrome, with many kinds of afflictions where people used to die quickly, can be taken care of and can maintain some reasonable life span. So this is a way to supplement government benefits. We have life insurance in a special trust called the Special Needs Trust so that those life insurance proceeds won't disqualify the beneficiary for any government benefit they might otherwise receive, and it won't be able to be claimed by the government to repay government benefits paid. This is a way to supplement the government benefits and to provide a fund to take care of their special needs in the future.

The other hot button—and this is big—is college education, or what I call a head start in life, not for the kids, but for the grandkids. Here is an interesting factoid that I think many of you may know. Often parents don't care as much about their kids as they do their grandkids. It's like what they say about the parents and the grandkids being the best of friends because they have a common enemy, right?

Here one of the things I talk about—and this is really important to look at doing—is a concept I call a family bank. Here is how I introduce it. I talk about the fact that the standard of living is going down. I always preface this by saying I'm just as patriotic as anyone else because I don't want them to think I'm criticizing America. But it's true, and we are seeing everywhere that the younger generation will be the first generation ever in the history of our country to have a decrease in their standard of living. It's true all around us.

For them to buy homes can be way more expensive than when you bought a home. For them to start a business, for them to save with higher taxes, for them to put their own kids through college—all of these things are far more expensive than they ever were before. I explain to the grandparent that these grandkids are not likely to have a head start in life unless you do something. Here is your choice. You can give everything to your kids and hope they will use it properly for your grandkids, or you can provide something directly for your grandkids that you know they will get, and you know they will appreciate, and it came directly from you.

By the way, that last part was really important. Did you hear it? That kind of legacy concept, a lot of people like that. So they now ask me, "How do I deal with this?" I say, "Well, you need a family bank trust." This is just a plain vanilla, irrevocable life insurance trust. One that allows the trustee to make discretionary distributions or loans to the beneficiaries as they need it for things such as buying a home, going to college, or starting a career. I explain that life insurance will be the funding of the bank. The life insurance proceeds will be deposited in this family bank trust. Your trustee will be your banker and will now stand in your shoes to make sure that those grandkids have the proper head start in life. Isn't that great? A lot of people like this concept.

Here is a variation on this ILIT concept, with the real estate owner. Those of you who have ever gone to real estate owners about life insurance may have run into some problems because real estate owners have this locked mindset that I put my money only in CDs until I have enough cash to buy another piece of real estate, right? I'm not going to put money in life insurance. Why would I do that? It's a poor investment compared to real estate. Well, of course, there is the estate tax issue, and they can be illuminated about that because if I say you got five pieces of real estate and two are going to go to the government, wouldn't you rather have all five go to your kids? That you've worked a lifetime to get to the current state?

The other thing I talk about doesn't motivate using life insurance for estate tax. I talk about using this to build your family's real estate empire. Would you like, Mr. Jones, to assure that you will build your family's real estate empire even after you are gone? This appeals to the real estate entrepreneur who, very often, is also a little bit ego-driven. And this is something I've utilized as a kind of a twist on the ILIT technique. The money in the family bank trust finances the purchase of more real estate.

Another bunch of overlooked uses in estate planning include stabilizing the legacy. What do I mean by this? Making up losses. We've got situations where you could say to someone, "I could help you make up the loss in your 401(k); I can make up the loss in your stock portfolio; I can help you make up the losses in other retirement plans or get back the tax you paid when you did the Roth conversion. Life insurance can replace these losses to your estate."

There's also estate maximization. I want to talk more about what's called the IRA stretch out. It used to be that if dad passed away, all the IRAs and plans went to mom. Mom died at age, say, 76. We went to a table, the table said mom had a six-year life expectancy, and the kids had to take all the money out and pay all the taxes in six years. Instead those non-spouse beneficiaries can use their own life expectancy for purposes of the taxable required minimum distributions. So if I'm age 40, I have a 46-year life expectancy. What I just said is that instead of taking it all out in six years, I can take it out in 46 years. And if I've got that period of time to compound money in a tax-exempt environment, am I going to do a lot better off later in life?

Keep in mind what we talked about just a few moments ago. The standard of living has gone down. And one of the things that I show people to get them emotionally involved in IRA planning is what you do with your IRA or your qualified plans is going to determine whether your kids will ever retire or not. Think about this. How many corporations, even the one you've worked for, have the same juicy 401(k) and other retirement plans now as they did then? They don't. They've all cut them back, right? And think about this—the next generation has not been a saver, an accumulator generation like the one before. So with less retirement benefit and less accumulation, how are they going to support themselves during retirement?

It's going to come down to inheriting your retirement plan and making it theirs. So this stretch out of required minimum distributions is a very important issue that we want to address. Let me talk about a number of different IRA planning opportunities that involve potential life insurance. Many of them also involve potential annuity sales too.

First, we have the dynastic IRA. Again you noticed how I use certain terms. If I say I want to talk to you about a dynastic IRA, what are they going to say? What are the first two words people are going to say? "What's that?" By the way, those are my two favorite words in the English language because when someone says *what's that*, the door is now open for me to explain what it is. This is why I use terms like *family bank* and some of the others you will see. Like with the charitable remainder trust, I never call it that. I don't even want charity to be involved in the title. I call it a tax-exempt trust or a capital gains bypass trust. And when they hear that, what will they say? What's that? Right.

So, what's a dynastic IRA? Another way I have been calling it is super stretch out. Would you, Mr. and Mrs. Jones, prefer that your kids and your grandkids get stretch out or super stretch out? Well, super stretch out, sure. What's that, right? What we're talking about is having the IRA skip the kids and go to the grandkids. We'll get back to the kids in a minute. Why? Who has a longer life expectancy, the child or the grandchild? The grandchild. The life expectancy of the child might be 40 years, but the life expectancy of the grandchild might be 75 years. That means your wealth in the IRAs can compound over a longer period of time. By the way, when I use the word

IRA, I also mean qualified retirement plans, such as 401(k)s, 403(b)s, 457s because they can be rolled into IRAs now or by non-spouses even after death. So I count them as IRAs too.

What are some ways that we can maximize the super stretch out with the grandkids? If we left it up to the grandkids to decide how much they are going to take out every year, how much do you think they're going to take out, the minimum or the maximum? The maximum. So we want to make sure that they allow the money to compound and take it out over their lifetime—that's the benefit to it. Here's where we can use something called the restricted beneficiary payout or restrictive beneficiary form. We place a qualified annuity inside the IRA account.

Here is what the restricted beneficiary payout says. It says when I pass away, my kids or grandkids will get payments every year. They will get just the required minimum distribution. They can't go in there and yank out the whole account and blow that income tax stretch out. They will get a minimum distribution over their lifetime. Some of these payout forms allow maybe another ten percent or another portion in case they need to draw a little bit more, but the idea is that this assures the stretch out. This assures that there will be retirement money later in life for that kid or grandkid. This is a really powerful technique in terms of marketing and selling annuities.

If every time you see IRAs, you see qualified plans, and you don't talk about this, you are really missing the boat because what you have to make prospects understand is that required minimum distributions are elective. What do you mean by that, Phil, I thought you used the word "required"? No, I said, "required minimum," because if you pass away and I inherit your IRA, do I only have to take the minimum amount or could I elect to yank the entire account out the day after you die? I could, right? And here is the disaster that happens. We've done statistical analysis, I've done these with renowned CPA Bob Keebler, and if they yank the account out prematurely, they will lose approximately one-third of the future value of the account. And by the way, what's the future value of the account? There is a great rule of thumb that the future value of the account, if it's stretched out fully, will normally be anywhere from four to six times its current value.

So if it's a \$100,000 account, the future value is from \$400,000 to \$600,000. And if they cash it in prematurely, they lose about \$150,000 to \$200,000. That's real money, isn't it? Okay, not to mention watch this double whammy. When they cash it out too soon, what happens? I see my name is on a beneficiary form like CDs and other accounts. I go and cash them out, no problem, little or no income tax. Then I go to where the IRA is held and I say, "Cash it out, give it to me." I don't realize it's taxable. By the way, there is no 60-day put back rule for a beneficiary after death. So what happens?

This is what I say to the parents. Your kids go in there with the best intention, but they don't know the rules and they see they are beneficiary. They take the money and what happens? It isn't until April 15 of next year when they are doing their tax return that the CPA tells them they owe \$100,000. But where is the money? What have they done with it? Either spent it or maybe invested it somewhere where it's illiquid and what a double whammy that now is, right?

So when you paint the picture of why, making sure to guarantee the stretch out because remember, the stretch out is elective, let's guarantee it. Let's make sure your kids or grandkids are going to have that future retirement benefit. That's the benefit of the restrictive beneficiary payout. Very powerful.

There is another technique utilizing what's called an IRA Inheritance Trust as the beneficiary. It can also make sure to guarantee the stretch out. The additional benefit is that it also wraps an asset protection shell around the inherited IRA because it makes it more difficult for the spouse to get it in a divorce, or for the lawsuit or creditors to get it. It doesn't pass through a second estate or cause a beneficiary to lose government benefits.

Normally, if the total amount of IRAs and qualified plans of the husband and wife together is less than \$150,000, then, in most cases, the restricted beneficiary payout is better because the cost, the expense of doing the trust, the complexity of the trust probably doesn't make sense. When the IRA is over \$150,000, you project out the future value to \$750,000, or thereabouts, and the need to also asset protect makes the IRA Inheritance Trust make sense.

Back to the grandchild example. We had the grandchildren here as IRA beneficiaries for super stretch out because they have a longer period of stretch out. What do the kids get? The kids get the life insurance in an irrevocable life insurance trust. Now, everyone comes out ahead, do you see that? That combo sale is terrific, and we've done a lot of those. Also, here in maximization of IRAs is what I call the super-leveraged IRA. And when I say super-leveraged IRA, what are the two words I hear back? What's that? I love it. Here the problem is that assuming it's not a Roth IRA, it's a regular traditional IRA, and when those beneficiaries take it out—even when it's stretched out—they are going to have to pay income tax. “And by the way, Mr. and Mrs. Jones, do you think our income taxes tomorrow are going to be worse than income taxes today?” What do you think they say 100 percent of the time? They are going to be a lot worse. So here I say, “What if we could allow those required maximum distributions or RMDs to essentially be tax free?” I have to say “essentially” because they are not actually tax free, but by the life insurance that we place there they now can pay the income tax on the RMDs.

Also, it can pay the income taxes if we do a post-death Roth conversion. This is something you may not know about, but this is going to happen sometimes where someone has a qualified plan, but they don't want to roll it out in an IRA during her or his lifetime mainly because of asset protection reasons. IRAs don't have the same condition protection as a qualified plan does, but it does get converted to an IRA—a Roth IRA—after death. And there is going to be income tax. At that point, the spouse or non-spouse beneficiaries have to pay the tax at their bracket. Think about this: A married couple, one dies, and now the survivor is doing the Roth conversion. Is the income tax bracket of that survivor higher than when she or he was married? Yeah, almost always because they were filing jointly before, right? So here insurance can pay the income tax as well.

I would put a star next to this IRA opportunity because this is something that many of you have heard of but have forgotten about. And this one is going to come back again because of what's happening to the estate tax exemption. With the estate tax exemption having grown from \$600,000 to \$5 million over the last few years, most people, including those with large IRAs, didn't worry about estate tax. But if that exemption drops to \$1 million, we are going to have a lot of our middle class clients affected. I'll give you a common scenario. A middle class client

has a home. He paid off the mortgage over the years. It's worth \$500,000 to \$1 million, to \$1.5 million in Southern California. If it's only worth that, then it's what we call a scraper. And here you start adding your other assets plus IRAs so they're over the million dollar exemption easy. What's the solution? Something we call the rescue plan.

Here I want to talk about where we have a QTIP, the QTIP rescue plan. Remember I said earlier that QTIP trusts are bad? A QTIP trust is an estate plan. It's typically done because you've got kids in more than one marriage or concerns about remarriage into the future, that kind of issue. They want to assure, the first to die, that their kids are going to get the estate after the survivor dies. I've already told you that it is not very good planning in general. But for an IRA it's worse. I want to share with you something that you'll love with this blended or mixed marriage. I'm going to share with you why QTIPs are for ears and not for heirs.

What I show them is that if your surviving spouse does not get the IRA directly, she or he gets it in a QTIP trust. This is a disaster for a whole bunch of reasons. First of all, if I'm the survivor, I can't defer the first distributions that are taxable until after I reach 70 1/2. I have to take the first distribution by December 31, year after death. Also, I cannot use the more favorable uniform distribution table that I could use in a rollover, that's basically a joint and survivor table. I have to use the inherited IRA table, which is going to force me to take the money and pay the tax more quickly. And if I live too long with these required minimum distributions coming up, I may strip the whole account, so there is nothing in there left for first-to-die's kids anyway.

And even if there is, those children will not be able to use their own life expectancies for stretch out purposes. Their RMDs will be based on the remaining life expectancy of that spouse. They will have to take it out quickly. On top of that, we've got accounting and investment rules that are a trustee nightmare because who are they favoring, the spouse or the remainder beneficiaries? And how do we account for income, and what kinds of investments can we do? What a giant nightmare and, of course, World War III between these two factions competing, the spouse and the kids of the first-to-die.

So again, where you see a QTIP trust, particularly a QTIP trust where the IRA is going to go in, this is a great opportunity for a life insurance sale. The perfect scenario would be that I'm the husband and it's my kids whom I want to eventually get it. Then if I can get a single life policy reasonably on me, I'm going to have that policy pass to my spouse. Why? Because who is the IRA more valuable to, a spouse with this life expectancy or kids with a longer life expectancy? Do you follow me? But what if I just can't get reasonably priced insurance, a single life policy? I have to go to a second-to-die type policy. Now here we would flip it and we would have the spouse get the IRA account and the children or grandchildren get the second-to-die policy through an irrevocable life insurance trust.

This leads me back to the IRA rescue plan. This is where you do have a potentially taxable estate including the IRA because the IRA is part of the taxable estate. It is not part of the probate estate because it passes by the beneficiary form but is part of the taxable estate.

What can happen here is that I see a large estate, a sizable IRA, and I ask the client, "Well, you've got \$500,000, \$300,000 in the IRA, what do you think is the chance that during your life you are going to pull out all the money in that account, not too good, right?" I say, do you think there might be—and I can pick a number—\$50,000 or \$100,000 here at the bottom that you will never touch? That's what we call bottom money. So guess what, if you leave that money in there, you are going to have a triple tax whammy when you die. What's that? Income tax (I'm assuming it's not a Roth)—federal income tax, state income tax, and federal estate tax. If you combine all three of those, you are talking about real money, you are talking about maybe 65 percent or 70 percent combined rate of tax.

So if you just leave that bottom money there, Mr. and Mrs. Jones, they are only getting 30 cents on a dollar, that's not very good. Why not consider this? Instead of this stretch out because Mr. and Mrs. Jones are just taking minimum distributions, why don't you use this strip out instead? What's that? Well instead, take out that \$100,000 at the bottom. Maybe we're not going to do it all in one year because of taxes. We're going to take that \$100,000 and we're going to put it into an immediate annuity that is going to generate a certain amount of after-tax income perfectly matched up to pay for the life insurance. Now we've got life insurance typically in an ILIT at

that point so the proceeds will be federal and state income tax free and estate tax free. This is a great combo sale, and we've forgotten about this technique because the exemption has been very high recently.

This also may be better than a Roth conversion. If you are looking at a Roth conversion where someone has a taxable estate and he is not likely to ever use the money, ask him if he is going to let that money compound in the Roth. He's going to say, "Yeah, I don't have to take minimum distributions from Roth, why not let it compound tax to free in there." That's going to be part of the taxable estate, that growing Roth, isn't it? What's interesting is there will be situations where you'll be able to blow out the other competitor because you are going to show the prospect with a taxable estate that the Roth conversion may not be as good as the strip out and purchase of life insurance. And it's easy to project these numbers. There are many software packages available to do this.

Another area of estate maximization is what I call the super-leveraged B trust. Do you know what I mean by a B trust? In most married estate plans, when the first spouse dies, some of it goes into a trust or directly to the survivor, that's the A, and the rest goes into an exemption or family or credit shelter trust known as B. I always explain this to my clients in a funny way, so they will always remember whose trust is which. The B stands for below ground, that's the first spouse-to-die's part, and the A stands for above ground, that's the survivor's part.

We set up the B to get the exemption amount of the first to die, so it's not lost. Even with the new portability unless there are lots of good reasons to still setup the B. Here is an interesting little twist. Let's say you have a client who is a surviving spouse, and either she is in the process of setting up this A and B or she already has it. You know the B trust can only have in it the \$1 million, \$2 million, or whatever the exemption is. If you can say to that surviving spouse, "How would you like it if I can increase the amount of exemption you could put into B from \$1 million to \$2 million?" How do you do that?

I'm going to use life insurance in the B trust because I am going to be careful if the surviving spouse is the trustee of the B or has powers of appointment over the B. You need to do this

correctly with an attorney. But basically the B trust can function like its own irrevocable life insurance trust. And you know what's great about this, who is paying the premium? Is it coming out of the survivor's pocket or is it coming out of the trust? You know and I know that somehow people don't feel like that's real money. It's just like they're IRAs. They don't have to write the check out of their personal account. When the check comes out of the IRA account, they are more willing to give that to you than they would a CD or checking account. So this is the way to compound and super leverage the B trust. It can be a combo sale. Why? Because you buy an immediate annuity in the B to pay the premiums for the life insurance. I've seen this use quite a lot because this is a key concept. The B trust can grow indefinitely; it doesn't matter what its size is when the survivor dies, it's not taxed. So this is a very important concept.

Another estate maximization concept is something I call the perpetual family legacy. Do any of you have clients who are do-it-yourselfers? You've got engineers, you've got doctors, you've got accountants, you've got egos. This is the kind of thing that appeals to the techie or the ego-driven person, the perpetual family legacy. It is basically a private foundation. What's interesting is that private foundations are no longer as expensive to set up and administer. There are lots of companies that do this for you very cheaply—for you and your clients. A private foundation can buy life insurance on the original donor or the creator that contributed into it. There are some limitations, but basically they can buy life insurance, so what happens?

When they pass away, the life insurance they bought will mature and will now be the funding of the family foundation that can perpetuate a particular hobby, a particular university, research, or a church—whatever it is that someone would like to leave as a legacy. Often it's a combo sale with an immediate annuity because inside of the private foundation they can buy an annuity to pay the insurance premium. And here what's interesting. They can involve their family, and we can make this even better because when they are putting the money in the foundation, it is tax deductible. It might be limited to 20 percent of adjusted gross income, but it's deductible. Don't you think that people like it better when you can show them how to make that insurance premium deductible so Uncle Sam picks up a third of it? Powerful stuff. Watch how this blows people's minds.

It's much bigger than this because here is what happens. Mr. and Mrs. Jones, you're going to have \$1 million policy on you, and when you die, the family is going to take that million dollars. They are going to invest \$500,000 of it for charitable causes because they have to pay out money for charitable causes from that foundation. But they are also going to take the other \$500,000 and they're going to buy life insurance on them. So now at the next generation level you're going to have \$5 million in the foundation, in the next generation level, \$20 million in the foundation, and so on. You've heard of the Fords and the Rockefellers? Ever watch PBS? It's actually a pretty simple thing to set up if you have an attorney. There also are companies that do this for you.

Now, here are a couple of estate tax wrinkles. One that we are running into in California is the nontraditional marriage. You know what I'm talking about, right? Same sex marriage. But it could also be where you have a heterosexual couple who live together but never get married. The problem for estate tax is can we get a marital deduction for what passes from one partner to the other? No, it's immediately taxed when the first dies, which can be devastating for the survivor. There's also the potential conflict between families where you can have a situation where I'm saying, my "spouse." I want to support that spouse during my lifetime, but when that spouse dies, I want it to go back to my other family members. We've got that same remaindermen issue, that same World War III kind of conflict between them.

One of the things we often do is to use life insurance, but we couple it with a charitable remainder trust. This could be a lifetime or a testamentary one set up at death. Why? Because we can put money into a charitable remainder trust where the survivor is now getting an income stream for the rest of her or his life, and it can even be an increasing stream over time. After she or he dies, the remainder will then go to charity. Because of that, it will be an estate tax or a gift tax charitable deduction somewhere like a marital deduction, but that charitable deduction is never 100 percent. So you still often will combine the charitable trust with life insurance in an ILIT. We're going to see more and more of these nontraditional married couples. These people need a way to figure out how to make sure their survivor is protected. So there you go back to a more traditional use of life insurance for a nontraditional couple.

Also, there's IRS audit insurance. I say to a client, How do you like getting audited by the IRS? Oh, my goodness, I hope that never happens. Well, how would you like getting audited after you die, where they can go back and assess penalties and interest and all kinds of things on gifts you made and other things you did? And, specifically, here I am talking about audit of the estate tax return itself. When I've got someone who has hard-to-value assets, such as a closely held business or royalty stream, we can see a big fight with the IRS over valuation some day. Or antiques that are hard to value. When you have assets like this, is the IRS going to argue the minimum or the maximum value they can support? The max, and now it becomes the war of the appraisers, and there could be a lot more estate tax than someone thought. They might need to have some insurance as backup.

Another use of life insurance is where we do aggressive lifetime or death planning such as deep discounting of the value of gifts using things like FLPs and LLCs, or we use a personal residence trust or GRAT or an installment sale. These are things I'm not going to get into. They're kind of mind-blowing, but they are for larger estates where we use techniques to get assets out of the estate during the client's lifetime. Those last three—the QPRT, the GRAT, and the installment note—if they don't live for a certain period of time, they have a significant value still taxed in your estate. So we want to cover that tax with life insurance. One of the neat things is we sell a lot of QPRTs. It's a way to move the house out of the estate where it has almost no effect on the owners at all. We can put your home in a QPRT where you have the right to live in it for life if it's structured right, and you have the ability to sell it and get the capital gains exclusion to get an income stream from it if you need it. You have all of those rights, but we get it out of your taxable estate. But there is a catch. You have to live for a certain period of years. If you don't, it comes back so during that period of time, we want to have life insurance, a sizable term policy, to cover the tax.

Everything I've talked about so far involves estate planning. But wouldn't you agree that most people are more concerned about what happens to them today than after they die? And the hot button for a lot of people is income tax. Let's look at some new ideas here, how you can create tax deductions using life insurance.

A defined benefit pension plan. Has anybody ever sold life insurance inside a defined benefit pension plan? This is a giant opportunity. As much as 50 percent of the contribution can go toward life insurance. And that is a deductible contribution, isn't it? When you show someone I can get a tax deduction where you are setting up your life insurance, that's neat, but where will we use this? We could use it even when someone is retired. It's actually better if they're older because they can put more into the retirement plan to fund their retirement benefit. Here is where I have someone retired or older in life set up a consulting company, a management company, as a lot of people are still consulting back with their old employer or they have a side business or they leave rental property that is a business. So they set up the consulting company. A portion of the income comes into the management company or consulting company. And now, depending on their age, we can usually get a contribution of up to 75 percent of that income into a retirement plan, and half of that contribution could go to life insurance.

This is a great way to utilize life insurance in planning and a possible annuity sale too because they've got other assets in the pension plan they're going to invest.

Also, there are ways to reduce taxable income and the double tax on social security because people have too much interest or other forms of income. That's a big opportunity for annuities, but instead here we're using life insurance. Maybe we front-end load a policy, we dump an entire CD or two or other accounts bearing taxable interest in it. If they need the money later, we take out tax-free zero cost policy loans if it's a non-MEC, modified endowment contract. If they keep the money in, they are essentially using income tax pretax money to pay the premiums because we're leaving it in the policy. So either way it's a leveraged use of their income pretax.

Insurance may also be used when avoiding capital gains tax. This is where I use the capital gains bypass trust or tax exempt trust. When I introduce this, what do they say? What's that? It's just a charitable remainder trust or CRT, but I don't call it that or hardly anyone would listen further. Many people are not aware this is something you should always ask during your interviews. Are any assets here real estate, stocks, business, or a home that's appreciated so you would consider selling today if you didn't have to pay a capital gains tax? You'd be surprised how many people say, yeah, I'd sell that darn property or yeah, I've been meaning to sell my home, but I've got

gain more than my capital gains exclusion of \$250,000 single or \$500,000 married. We can use the CRT to sell all sorts of assets capital gains tax free. At some point their remainder is going to go to charity, so how do we replace that to the family? With life insurance.

Here's a neat CRT concept I want to share with you called a home buydown. This is an actual case I had. A couple had a home that was worth \$1 million. They wanted to sell it, but they had far more than the \$500,000 married capital gains exclusion. In fact, they had about another \$400,000 of capital gains that would get taxed. What a lot of people don't know is you could sell only part of the property with the CRT. We sold half of the property directly—the title still stayed in the clients' name. With that half they used their \$500,000 exclusion and paid no tax. They took \$200,000 and stuck it in the bank, and with the other \$300,000 they bought a retirement condo free and clear. So far so good. They pay no income tax on the other \$500,000 that's in the CRT, and now they have a stream of income for their life on that entire \$500,000. Do you think these clients are happy? They've got \$200,000 in the bank that they can play with, they got a paid up home, and they got a stream of income on \$500,000 in the CRT. That is a very happy couple.

Now, of course, we know the glitch is that the remainder of that \$500,000 will go to charity. If they want to replace it, that's where the life insurance comes in and possibly a combo sale of annuity inside of the CRT. That's a very powerful technique.

Here is one other little CRT wrinkle. I am in the process of closing one of the largest life insurance cases I ever had, and this is one I would say would escape 99.9 percent of people when they look at the scenario. I have a very wealthy guy. He has a big municipal bond portfolio. He hates life insurance, he doesn't want to pay for life insurance, and he thinks that municipal bonds are the only conservative, smart thing to have. I showed him what happens when we take that \$2 million municipal bond portfolio and put it into a CRT. When we do this we're not doing it for capital gains reasons. He is still going to get all the income coming out of that trust like he did before. It will still be tax exempt when it comes out, and he can reinvest those bonds when they mature inside the CRT. He is going to still get all that tax exempt income. But what did it just generate when he put those municipal bonds into the CRT? He got a large income tax deduction.

At his age we were able to get him a giant income tax deduction the way we structured the trust, and now we're using those tax savings from the income tax deduction to buy the life insurance that will now more than replace the remainder of that trust. This is a guy who would never ever have bought life insurance, but when I showed him how he is basically getting free life insurance, no catch. It's paid for out of tax savings he didn't have before. If you hold on to it you get nothing—no deduction, no insurance. This isn't for everyone, but if you ever run across a large municipal bond portfolio, this is awesome.

Now let's talk about retirement planning. Here is one technique that some of you are aware of. It's called pension maximization. Some retirement plans only allow an annuity option as their payout, they can't do a rollover. They give you either a single life or a joint life annuity. Yes, there are still a lot of plans out there that have this. Now, what happens is you twist logic on the client. You say, "Would you rather have just an income for your life and then when you die your survivor has nothing, or do you want the joint and survivor benefit?" They always will say they want the joint and survivor benefit, but the joint and survivor benefit is less per month. It is less per month because the pension people are basically buying life insurance on you with the difference. So if we can beat that difference, wouldn't you rather do it yourself? We keep the single life benefit, we then pay the insurance premium from that, and we show them that now they are going to get much more than they would have under the joint and survivor option while he's living and when he dies, his wife gets the life insurance, which also generates a bigger income stream. So this pension maximization is sometimes very powerful.

Another retirement planning technique is what I call pension replacement or the private retirement plan or supplemental retirement plan. What's that? We use a single premium or front-end loaded policy, and we allow for tax-free withdrawals later in life. I've used this with people who have already maximized their pensions. I did this with a high-paid athlete who wants to have more of a pension later.

Another retirement-related item here is a biggie. It's a kind of policy that is sometimes called single deposit life insurance. I found over time this is the absolute easiest insurance sale when

you really help the clients, during their lifetime, delay with the cost of long-term care. The problem with traditional long-term care insurance is that it may not be possible to get depending on age and health. It can be too expensive, and it's use it or lose it. If you pay those premiums quarterly for your life, whatever you don't use does not go back to you or your family. What other ways can you look at dealing with this? One is a long-term care rider on a life insurance policy, or on some annuities. But that typically still has ongoing premiums, which people don't want to pay. A better way is to show them the single deposit life insurance that I call single deposit life. Here is the story I tell them.

Let's say you have \$100,000 in a CD. We then move that \$100,000 CD into a single deposit, one-time premium life insurance policy. You are going to be better off because the interest income generated inside of the life insurance policy is not taxed. It may be taxed later when you take it out, but it's not currently taxed, which may also reduce the tax on your social security income. In addition, you have guarantees that you can take out the entire amount at any time without penalty. Can you do that with a CD? No. What happens now is you have \$100,000 in the life insurance policy, but the insurance company gives you an additional \$100,000 to \$200,000 of long-term care benefit. What's even better is that if you don't use it, your family gets that benefit. If there was \$300,000 of benefit and you didn't use it, your family would receive it as an income tax-free death benefit.

Now, I know those numbers could vary. I'm just giving a broad example. This can also be used in conjunction with a long-term care insurance policy to save on premiums. Here is one way I've sold it. The client has long-term care insurance already. I'd ask, "How would you like it if I could cut the cost of your long-term care insurance in half?" Oh, wow, how do I do it? Well, you open a single deposit policy and now extend the waiting period on the long-term care insurance policy because the single life deposit policy can bridge that gap period, that waiting period. So we can move the waiting period out, which reduces the premium cost. That's a really cool tandem sale. It's easy to explain to clients how it works, conceptually, like I did.

Keep in mind that you can do a tax-free exchange of an existing life policy. What am I talking about? Somebody has a policy. He has some cash surrender value in it. I say, "How would you

like it if I could turn this policy into one that not only has as much death benefit, but also gives you a long-term care benefit while you're alive, and it doesn't cost you anything? Would you be interested in that?" That's a very powerful way to sell a particular kind of life insurance.

Also I am going to say that one of the ways you will generate a lot of insurance sales is by reviewing existing policies. I want to give you a tip here. If you come across someone who has an insurance policy in an irrevocable life insurance trust, there is a way that you almost always get a review. Here it is. You can say to them, "Did you know that your trustee has potential liability and there have been court cases on this?" If they don't review that policy periodically and make sure it maximizes the death benefit, those beneficiaries can sue that trustee some day and get it out of their personal pocket. This has happened; this is real. The need to periodically review those policies is tremendous. What has happened? With new life expectancy tables, with new census tables, we're finding we can rewrite old policies that were and very often do a clean exchange with no more premium going in and get more benefit.

When reviewing old policies, we also can consider a life settlement if they are over 75. Here is one way I explain this to clients. This is a true case. I had a little old lady. She had a \$1 million policy, and she was paying \$50,000 a year premium. She said, "Mr. Kavesh, I don't want to pay this premium anymore. I just can't afford it. I'm just going to let it lapse." I showed her that this could be a big mistake because even though there might be cash surrender value, she could do a lot better with the life settlement. So we sold the policy, took the proceeds, put them in a new paid-up policy for \$1.5 million. She had a \$1 million policy that she was paying \$50,000 on. She wound up with a \$1.5 million policy that is completely paid up with no more premium. Do you think that was a happy client? Here is what I say to my client who I've just told this story to, "I don't know if this applies to you, but isn't that worth checking out? Hopefully, I'm giving you some tips that can help you break through the gap here.

Here is an interesting retirement planning use—a guaranteed retirement plan for the children or grandchildren. This is kind of the reverse of what you would think, where the child buys it on the parent. What if the parent lives too long and the child needs money? She or he could borrow,

maybe do a life settlement later as the parent gets older or the parent could buy it to fund the grandchild's retirement like in the family bank trust that I talked about.

The last thing I want to talk about is really important. I'm going to stress the importance of working with a qualified estate planning attorney when you propose life insurance. Using a life insurance trust is clearly the best way to hold life insurance for virtually all clients. It's much better than having the insured own it themselves or have the beneficiaries own the policy. There are two key words, control and protection. Control by the insured can be maintained because, if the policy is an irrevocable trust, they can make sure the premiums are getting paid. They can make sure the beneficiaries don't prematurely cash out the policy or use it for something else stupid. And in an irrevocable life insurance trust that is written carefully with provisions, called trust protector provisions, we can indirectly make changes to an irrevocable trust. Isn't irrevocable a dirty word? Because irrevocable means not changeable, right? I tell people I have a flexible irrevocable trust and what do they say? What's that? My flexible irrevocable trust allows a third-party, not a relative, but maybe an attorney, financial advisor, accountant, or friend non-related by blood, to be able to make changes to the trust in a way that doesn't cause those trust assets and insurance to come back into their estate as the original insured. The client can still change trustees, change beneficiaries, as well as when and how they get it. But there is also enhanced asset protection for both the insured and the beneficiaries. This is really important because what the insured doesn't understand is that if I had beneficiaries on the policy, and if they get sued, divorced, or whatever, they can lose the policy. But if the policy is in an irrevocable trust, it's protected from those predators.

Also, there's the idea of a dynastic trust that can pass down for generations. This is really appealing to a lot of people—that level of protection going on for multiple generations. Second estate tax as each generation dies is very important. One of the overlooked benefits of an ILIT is that those proceeds are not taxed again in the children's or beneficiaries' estates, the trust money can be compounded. Remember I talked about financing the family real estate empire and using the ILIT now as an investment vehicle that continues to pass down tax-free. Here's my point. You definitely wouldn't want me to testify if you're selling life insurance of any reasonable amount, meaning if it's over a couple hundred thousand of life insurance. You should almost

always have it owned in an ILIT. Because, quite frankly, isn't it malpractice if you don't at least recommend an ILIT? If I were you, I'd have the clients at least sign off that you recommended an ILIT if they're not going to do it, as your own protection.

Let me cut to the chase now as I'm finishing up. The moral of the story is that you can almost always find a legitimate use for life insurance as a solution to a client's particular problem if you look closely enough. Become a problem solver rather than a product pusher. It's better for the client and the heirs, and it's better for you.

I want to return to what I said at the beginning. When you talk to clients about issues and solving issues, even if you didn't sell the life insurance for whatever reason, that's okay. You looked at an issue and proposed a solution that they never heard from anyone else. Are you going to have more credibility? Are you now going to be able to do the other things, to sell other things that you may want to have the opportunity to do because you've got the attention and the respect and the authority with that client? And if you do sell insurance when clients die, what is going to happen with the life insurance proceeds, especially if they've got it in an ILIT, especially if they've got a relationship with the attorney and the accountant whom you are working with on the ILIT? You've just created millions more of potential assets under management or potentially going into annuity sales. So when you see the whole picture, utilizing life insurance is tremendous for the client, the next generation, and your business too.

Where do we go from here? Did anybody learn something new today they could use? Great, please use it and really help people while also increasing your insurance sales.