John Hancock

Success Story

Advanced Markets

Planning in Action

Leveraging gifts with commercial financing

Case in point

A producer called into Advanced Markets to discuss a high-net-worth client in need of substantial life insurance. The majority of the client's wealth is contained in hotel ownership. The client's business is currently experiencing cash flow issues, but the situation is expected to be short-term and there is an expectation that the business will see future growth. We discussed a commercial finance arrangement that would minimize the upfront cost to the client while also building in a repayment strategy that would not expose the client's assets to liquidation.

Designing a case & creating a plan*

Advanced Markets designed an Accumulation IUL policy with:

- An initial death benefit of $15M, Option 2 switch to Option 1 in year 12.
- Annual loans of $1,242,354 for 12 years. Crediting rate for AIUL is 6.05% using Core Capped A/C Vitality Bronze. Annual Loan interest starts at 2.5% increasing by 20 bps annually.**
- There is a policy withdrawal in year 17 equal to the principal loan balance due of $14,908,242 to repay the lender. Interest is being paid in arrears annually by the assets in trust.***
- For the purposes of the illustration we show a gift to a generation-skipping trust equal to the exemption limit of $11,580,000 of business interest to the irrevocable life insurance trust.
- Cash flow from the asset will pay the loan interest annually.

Client profile

- Current net worth in excess of $30M
- Business valued at about $20M
- Both children are involved in the business
- Client also has four grandchildren

The client's objective is to ensure there is sufficient estate liquidity to pay for any settlement costs as well as minimize or reduce the size of the taxable estate, while keeping the business in the family for generations to come. The client is also concerned about the uncertainty relative to the estate tax exemptions being reduced in the future.

Fact Finding

- Male, age 65
- Preferred Non-Smoker

The client needs $15M of life insurance. His current cash flow is low, but he feels we can assume 3.5% average cash flow from the business and with average appreciation of 6.5%. Client has not used any of his $11.58M lifetime gift exemption.

Why it works

Several significant wealth planning strategies are achieved with this technique:

- An immediate reduction of the gross estate equal to the exemption limit will reduce the future tax burden at the death of the Grantor. If the Attorney for the client feels this gift can be discounted for minority-interest purposes for example, the gross gift could be increased by the amount of the discount (assume a $16.5M gift discounted by 30%) further reducing the client's taxable estate.
- Current cash flow limitations are supported by currently low lending rates (assume 2.5% year 1) which means the first year's loan interest due on a $1,242,354 premium loan is $31,059.
- All future growth and appreciation on the business is held in the dynasty trust. By life expectancy of the insured, the value of the business is projected to be over $82M. All future growth escapes estate taxation in the client's estate.
- The dynasty trust will essentially "own" the business while the children and grandchildren can operate it without exposing the business to estate taxation in their respective estates.
- The life insurance policy is projected to repay the lender from the cash value buildup which prevents the trustee from having to "liquidate" any business holdings to retire the debt.

This design will reflect an increase on the total return to the heirs of over 9.35% at life expectancy. Current cash flow deficiencies are addressed using financing at low current rates and the business is held in trust for the benefit of the client's children and grandchildren, preserving the legacy the client created.

Call Advanced Markets at *888-266-7498, option 3* to speak with an Advanced Markets Consultant, or email *advancedmarkets@jhancock.com*

*This is a supplemental illustration. Not all benefits and values are guaranteed. The assumptions on which the non-guaranteed elements are based are subject to change by the insurer. Actual results may be more or less favorable. The non-insurance figures are also non-guaranteed.

**Actual loan interest may vary. Client's should work with their financial professionals to understand the underlying variables that may impact their actual plan.

*** Assumes the use of an indexed loan which carry more risks than standard loans in IUL policies.

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Loans and withdrawals will reduce the death benefit, cash surrender value, and may cause the policy to lapse. Lapse or surrender of a policy with a loan may cause the recognition of taxable income. Policies classified as modified endowment contracts may be subject to tax when a loan or withdrawal is made. A federal tax penalty of 10% may also apply if the loan or withdrawal is taken prior to age 59½.

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