



Life Insurance Premium Financing

A strategy that may help protect what's important while maintaining assets with higher growth potential.



A potential strategy for high income and high net-worth individuals.

Over the years, you have worked extremely hard to build what you have today. Creating your wealth has been a product of hard work, timing and utilizing your knowledge of your financial options.

It's likely that you have life insurance to protect your loved ones financially should you die unexpectedly. However, some life insurance can also be a valuable tool in supplemental retirement income, business succession, buy-sell arrangements, estate and legacy planning.

As a high net-worth individual or business owner, you may not have adequate liquid capital to pay premiums of a large cash value life insurance policy. In many cases, those funds are allocated elsewhere to increase your overall assets or grow your business.

This is where life insurance premium financing may be an option to explore. Additionally, there are potential tax advantages for a business owner through premium financing, depending on the structure of the loan arrangement.

How does premium financing work?

Premium financing is a financial arrangement through which qualified clients (usually those with high incomes and/or high net worth) purchase life insurance without liquidating other investments. Through this financial arrangement, qualified clients borrow the funds for the life insurance premiums from a third-party lender. Most life insurance premium financing arrangements are designed in such a way that the cash value growth in the life insurance policy can be used to exit the premium finance strategy and pay off the loan. If there is a loan balance at the client's death, part of the life insurance death benefit would repay the loan and any remainder could pass to the client's beneficiaries.

This strategy may enable the client to protect their net worth and pass their financial legacy on to future generations without altering their other financial strategies. While the concept of premium financing is simple, the actual transaction can be quite complex. For this reason, it's critical to involve your own qualified tax and legal advisors in the process. You want direction from people who understand the concept thoroughly and can assist you in determining if there is a premium financing option that fits your unique needs.

Each premium financing arrangement is custom designed to meet your unique financial goals. Premium financing transactions usually consist of two separate financial instruments: a life insurance policy and a third-party loan, illustrated in these three steps.



Step One — The Application for a Life Insurance Policy

The client completes an application for life insurance that includes both medical and financial underwriting information. The insurance professional submits the application to the insurance carrier, who determines if the applicant qualifies for the policy. In some instances, information applications may be submitted to multiple carriers to see which is an appropriate fit.

Step Two — The Application to Borrow the Premiums

After the life insurance policy is approved, the case is submitted to the most suitable lender for life insurance premium financing. The lender analyzes the applicant's credit and financial status and decides whether to make the premium loans. If the life insurance company and the lender approve both applications, the premium financing arrangement is typically underway. The lender will deliver funds for the life insurance premiums, and the client pays the lender interest charges and loan fees.

Step Three — Exiting the Premium Finance Plan

Repayment of loans associated with premium financing must be considered and careful planning should be contemplated in advance to ensure a source of funds for this purpose. In many cases, the policy is designed to carry cash value that will be enough to use to pay off the loan at some future point in time.



Some Potential Benefits of Premium Financing

If premium financing is the right fit, it may provide some of the following potential benefits:

- Lower out-of-pocket cash flow compared to traditional funding
- Less impact on existing personal assets, because you are not required to liquidate assets in order to fund the life insurance premiums
- Greater leverage of existing assets by continuing to employ them in an existing financial strategy
- Individuals and business owners may find tax advantages depending on the loan arrangement
- Utilizing a loan for premiums may significantly lower income taxes paid on premiums as the loan is not considered as income for tax purposes

Some Potential Disadvantages of Premium Financing

There is risk involved in any borrowing arrangement, and premium financing is no exception. You should regularly monitor your premium finance arrangement and be aware of these potential disadvantages:

- The life insurance policy and interest credited to the policy may not perform as projected, which could make the premium financing arrangement less beneficial for you over time
- The risk that the interest rates on the premium financing loan may increase, which could decrease the benefit of the premium financing arrangement and lead to the need for additional collateral or a decreased death benefit
- If the premium finance loan is called and the policy values are insufficient to pay off the loan, the outside collateral may be called, creating potential tax issues
- Interest on premium finance loans is generally not tax-deductible for individuals

Eligibility for Premium Financing

Because of its complexity, premium financing is not for everyone. If you are financially sophisticated and you have skilled tax and legal advisors, this strategy may be appropriate for you. Additionally, many Life Insurance companies and lenders require that you meet certain eligibility requirements. In general, to qualify for a premium financing arrangement, you may need to:

- Meet minimum net worth and/or income requirements
- Have a need for life insurance
- Meet life insurance policy underwriting guidelines
- Meet the lender loan guidelines

Important Issues in Premium Financing

There are several important issues that you should explore before considering a premium financing arrangement. A comprehensive examination of all relevant issues is beyond the scope of this brochure.



Legal and Tax Considerations

Premium financing has tax implications in several areas, including estate, gift and income taxes. You should consult with qualified legal and tax advisors that are familiar with these products to help you navigate through these issues. You've worked hard for your financial success, and it's important to protect what you've earned. Premium financing may offer a way to protect your financial legacy without forcing you to dramatically change your current financial situation.

There are several types of premium financing designs — including policies owned by an irrevocable life insurance trust, a business, or an individual.

Collateral Considerations

Sources of Collateral

All premium finance arrangements require collateral for the total amount of the loan. The policy's cash value typically covers the majority of the collateral; the remainder can be secured through asset options such as:

- Letter of credit
- Cash value of separate existing life insurance policies
- Brokerage accounts
- Cash



Work with an Experienced Insurance Professional

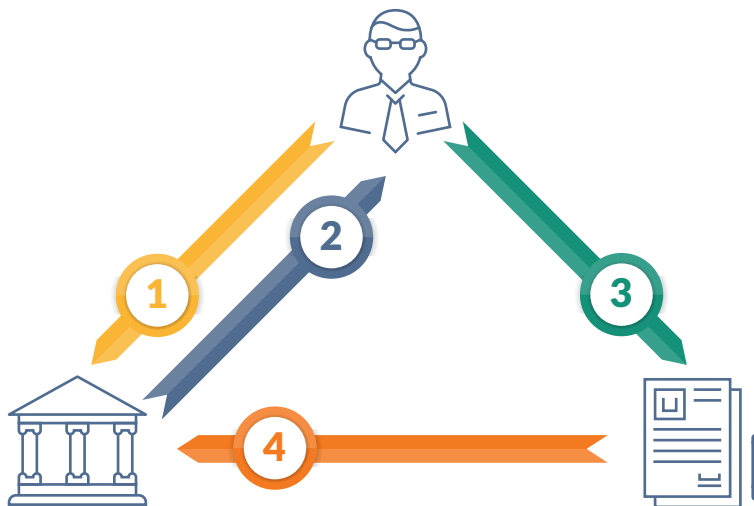
This brochure includes the basics of premium financing and a brief discussion of important issues, but doesn't cover everything you should explore before using a life insurance premium financing arrangement.

It is critical to get advice from an experienced insurance professional. Working with professionals may allow you to fashion a premium financing arrangement that suits your needs and helps you achieve your financial goals.

Below is an example of a typical premium financing case.

Mr. Smith works with the lender to work out a payment schedule. Mr. Smith uses those funds to pay the premiums on the life insurance policy. Upon loan maturity an amount equal to the cumulative loans due the lender is borrowed from the life insurance policy. Those funds are used to pay off the loan. The lender will release any collateral assignment upon repayment. (If, in this example, the policy values were insufficient to pay off the loan, the outside collateral may be called instead of released.)

- #1** Mr. Smith pays interest and provides collateral to the bank.
- #2** The lender loans premium to Mr. Smith.
- #3** Mr. Smith pays the premium to the insurance carrier.
- #4** Insurance carrier assigns the policy to the bank up to the amount of the loan.



Talk to us if you may be interested in using premium financing to protect what's important while maintaining higher-yielding assets.



Clarity Financial Wealth Management
440 E Huntington Drive, Suite 300
Arcadia California 91006
1.800.783.4951 ClarityFinancialins.com

Life insurance guarantees are backed by the financial strength and claims-paying ability of the issuing insurance company. Life insurance typically requires health underwriting and, in many instances, financial underwriting. Policy loans and withdrawals will reduce available cash values and death benefits, and may cause the policy to lapse or affect any guarantee against lapse. Additional premium payments may be required to keep the policy in-force. Withdrawals are generally income tax-free, unless the withdrawal amount exceeds the amount of principal paid.

**This example does not represent any specific product nor reflects sales charges or other expenses that may be required. This example is merely a hypothetical and may not reflect the process for some life insurance premium financing arrangements.*

This brochure is not designed to give tax, legal or lending advice. The information is general in nature and not comprehensive; the applicable laws change frequently. The strategies suggested may not be suitable for everyone. You should seek advice from your tax and legal advisors regarding your individual situation.

These materials are not intended to and cannot be used to avoid tax penalties, and they were prepared to support the promotion or marketing of the matters addressed in this document. Each taxpayer should seek advice from an independent tax advisor.

There are risks involved with premium financing that you should consider. Loan interest rates may rise and may force you to liquidate assets to pay such rates or be at risk of loan default. Similarly, the lender may require additional collateral if the value of posted collateral falls and/or if policy crediting rates drop. Finally, if you have failed to repay at loan maturity, perhaps because a planned exit strategy failed, the loan would default. If the loan defaults, the lender may foreclose on collateral, including the policy, and negatively affect your credit rating.

Exclusive rights to this material belong to GPS. Unauthorized use of the material is prohibited.