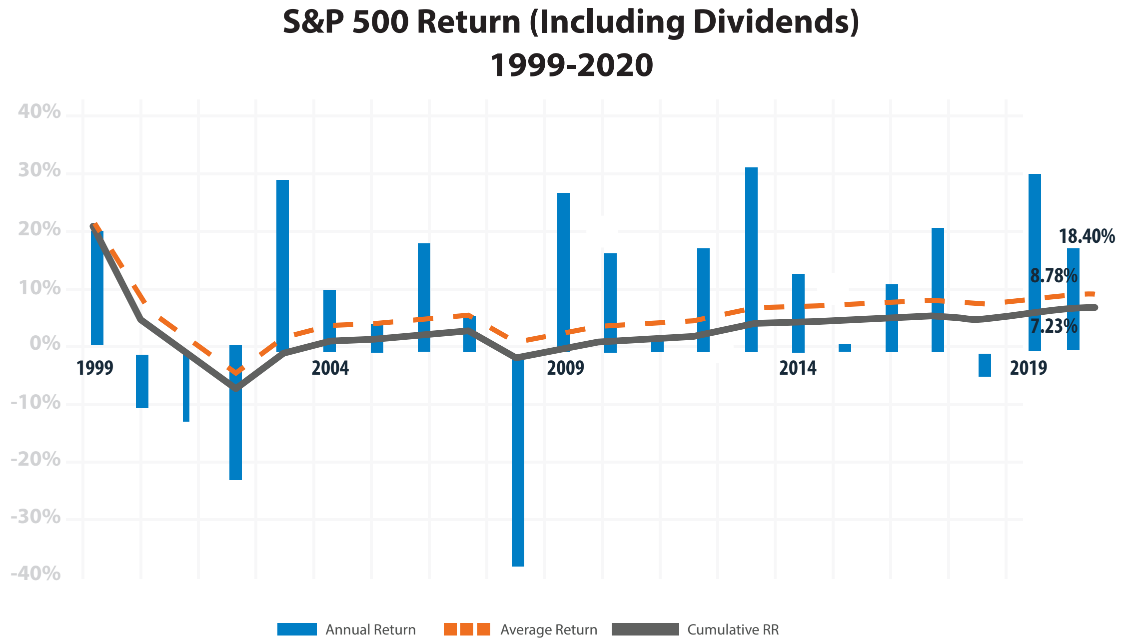
Life Insurance as an Asset

The value of an investment portfolio is subject to market fluctuations. The amount of wealth ultimately transferred to heirs is based on the value of an individual's investment portfolio at an indeterminate point in the future. Depending on the performance of the investment portfolio, one's beneficiaries may receive more or less than expected.

Many people remain uneasy about the financial markets after the 2008 market crash. A badly timed down market can devastate a planned legacy for years. The chart below details market fluctuations over a 22 year period, based on the S&P 500® Index, including dividends and before income taxes. Although the average return for the period is 8.78%, because of the sequence of returns, the cumulative return is 150 basis points lower at 7.23%.



MITIGATING MARKET FLUCTUATIONS

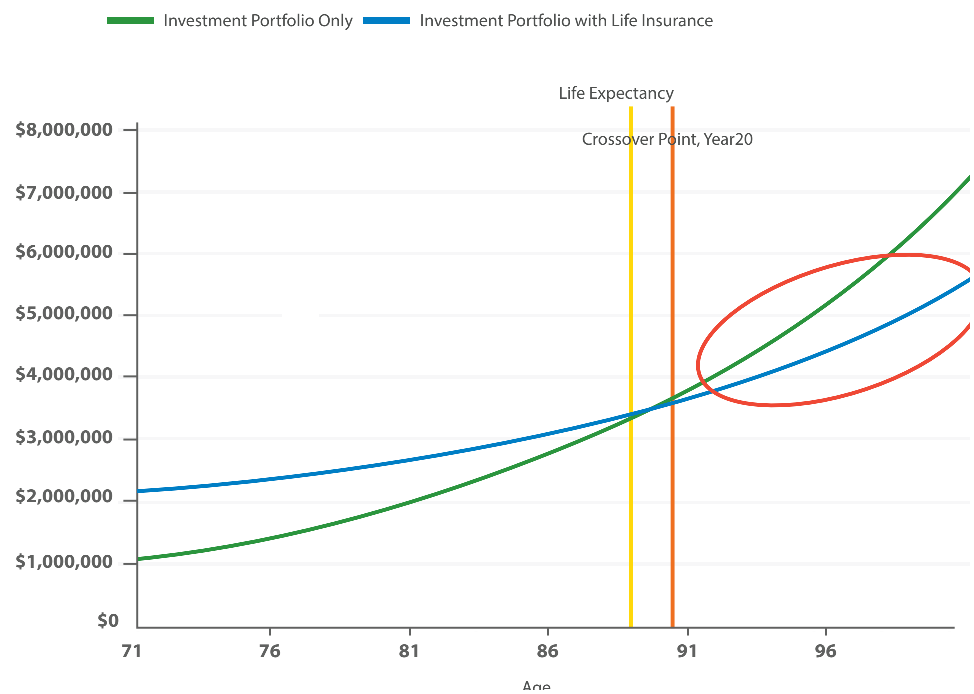
Life insurance is a unique asset in that the death benefit risk is borne by the life insurance carrier, which pays the death benefit in full at the event of death no matter what the timing. As a result, life insurance can provide a death benefit that is uncorrelated with other sectors of the investment marketplace, such as equities or bonds. In other words, the death benefit is based on the event of death — not a market event that can cause a downturn in value.

Life insurance is an asset that can ensure that there is an inheritance to pass on, regardless of how other assets perform. By allocating a small portion of one's portfolio each year to life insurance, individuals can smooth out the volatility in their portfolio and safeguard their desired legacy.

IMPACT ON PORTFOLIO AND WEALTH TRANSFER HYPOTHETICAL CASE STUDY

Harold is a 70-year old widower with a $1 million investment portfolio that he plans to leave for the benefit of his two children. He is concerned that his portfolio may not perform as expected, meaning that his heirs could inherit substantialy less than he anticipates. His financial advisor explains that by allocating a small portion of his overall portfolio to life insurance premiums he can smooth out the volatility in his portfolio, thus ensuring the legacy he desires for his children.

As a preferred nonsmoker, Harold has a 20 year life expectancy and wonders how adding a life insurance policy might enhance his overall portfolio. To understand the potential net to his heirs, the chart below assumes a $1 million portfolio invested at a constant 7% after-tax rate of return versus incorporating a $1 million dollar death benefit for an annual premium of $25,029 — approximately 2.5% of Harold's initial portfolio. Based on his assumptions, Harold would need to survive to his life expectancy for the investment only scenario (circled in red) to outperform incorporating life insurance into his planning.



The life insurance death benefit offers substantial leverage during the early years of the policy. At some point, the value of an investment portfolio only may exceed the investment portfolio plus death benefit, but this occurs around his life expectancy. While the investment portfolio plus life insurance is reduced by the amount of the premiums, the life insurance death benefit adds a stabilizing element to Harold's wealth transfer strategy.

Harold decides that the potential gain to heirs of the investment portfolio only, around his life expectancy, is not worth the risk of experiencing a market downturn at the wrong moment — an earlier death.

THE BOTTOM LINE

By allocating a portion of the investment portfolio to purchase a life insurance death benefit, it's possible to mitigate market losses and increase the amount of wealth transferred to beneficiaries.