Harmony Wealth Strategies
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Harmony Wealth Strategies
BUILDING AND SAFEGUARDING YOUR FINANCIAL WORLD

Life Insurance and Estate Planning

Life Insurance and Estate Planning

Life insurance has come a long way since the days when it was known as burial insurance and used mainly to pay for funeral expenses. Today, life insurance is a crucial part of many estate plans. You can use it to leave much-needed income to your survivors, provide for your children's education, pay off your mortgage, and simplify the transfer of assets. Life insurance can also be used to replace wealth lost due to the expenses and taxes that may follow your death, and to make gifts to charity at relatively little cost to you.

To illustrate how life insurance can help you plan your estate wisely, let's compare what happened upon the death of two friends: Frank, who bought life insurance, and Dave, who did not. (Please note that these illustrations are hypothetical and do not represent any specific products.)

Life insurance can protect your survivors financially by replacing your lost income

Frank bought life insurance to help ensure that his survivors wouldn't suffer financially when he died. When Frank died and his paycheck stopped coming in, his family had enough money to maintain their lifestyle and live comfortably for years to come.

And since Frank's life insurance proceeds were available very quickly, his family had cash to meet their short-term financial needs. Life insurance proceeds left to a named beneficiary don't pass through the process of probate, so Frank's family didn't have to wait until his estate was settled to get the money they needed to pay bills.

But Dave didn't buy life insurance, so his family wasn't so lucky. Even though Dave left his assets to his family in his will, those assets couldn't be distributed until after the probate of his estate was complete. Since probate typically takes six months or longer, Dave's survivors had none of the financial flexibility that a life insurance policy would have provided in the difficult time following his death.

Life insurance can replace wealth that is lost due to expenses and taxes

Frank planned ahead and bought enough life insurance to cover the potential costs of settling his estate, including taxes, fees, and other debts that his estate would have to pay. By comparison, these expenses took a big bite out of Dave's estate, which had to sell valuable assets to pay the taxes and expenses that arose as a result of his death.

Life insurance lets you give to charity, while your estate enjoys an estate tax deduction

Using life insurance, Frank was able to leave a substantial gift to his favorite charity. Since gifts to charity are estate tax deductible, this gift was not subject to estate taxes when he died. Dave always dreamed of leaving money to his alma mater, but his family couldn't afford to give any money away when he died.

Life insurance won't increase estate taxes — if you plan ahead

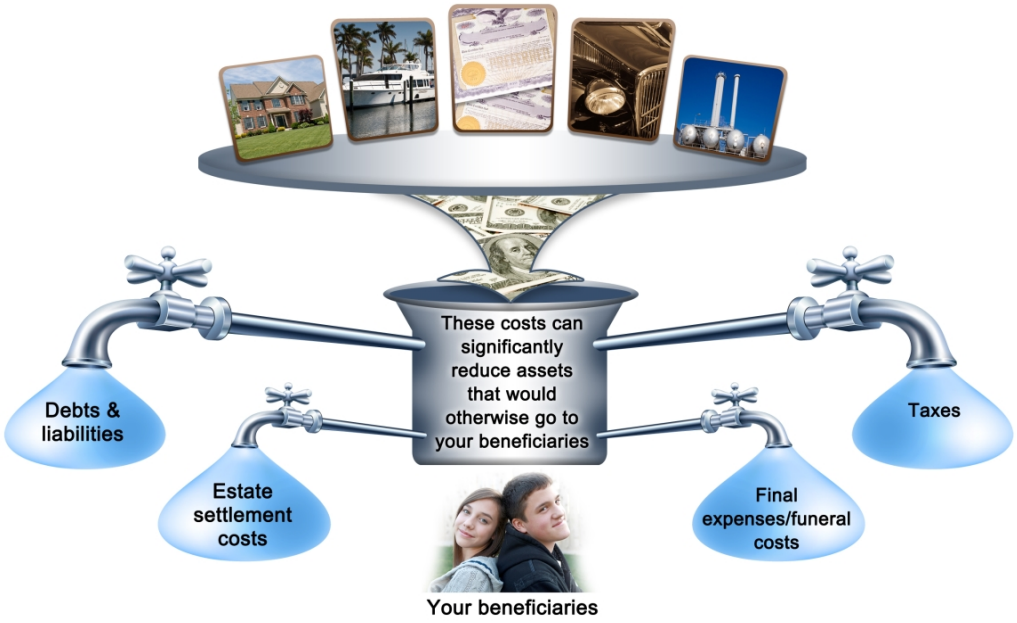
Before buying life insurance, Frank talked to his attorney about the potential tax consequences. Frank's attorney told him that if his estate was large enough, it could be subject to federal and state estate taxes, depending on the applicable law at the time of his death. Frank and his attorney put a plan in place that would allow Frank's survivors to use his life insurance policy to help pay for some of the potential estate taxes that might be owed at his death.

Be like Frank, not like Dave

Throughout his life, Dave worked hard to support his family. Frank did, too, but went one step further — he bought life insurance to protect his family after his death. Here's how you can be like Frank:

- Use life insurance to ensure that your family has access to cash to help them meet both their short-term and long-term financial needs
- Plan ahead — buy enough life insurance to cover the potential costs of settling your estate and to ensure that the assets you leave to your survivors aren't less than you intended
- Consider using life insurance to give to charity
- Consult an experienced attorney about income and estate tax consequences before purchasing life insurance

Estate Shrinkage



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Irrevocable Life Insurance Trust (ILIT): A Wealth Replacement Trust

Definition

An irrevocable life insurance trust (ILIT; pronounced "eyelet" and also called a wealth replacement trust) is a trust that is funded, at least in part, by life insurance policies or proceeds. It is an effective estate planning tool that, if properly structured, may help avoid generation-skipping transfer, gift, and estate taxes, while providing a source of liquid funds to your estate for the payment of taxes, debts, and expenses. An ILIT can be either funded or unfunded.

Prerequisites

- You want to avoid generation-skipping transfer, gift, and estate taxes or provide liquidity to your estate
- You are insurable
- You execute an ILIT agreement
- You transfer title to all contributed assets
- You amend any existing contracts and documents to reflect the trust as the real party in interest

Key strengths

- May help avoid generation-skipping transfer, gift, and estate taxes
- Takes advantage of the annual gift tax exclusion
- Replaces wealth to provide for your family
- Provides cash to your beneficiaries so that your business can continue to operate after your death
- May provide funds for the costs of settling your estate (if the estate is in a position to sell assets to the trust or repay a loan, with interest)
- Provides for professional management of your assets
- Avoids probate
- Maintains your privacy
- Trust assets may be protected from estate creditor's claims

Key tradeoffs

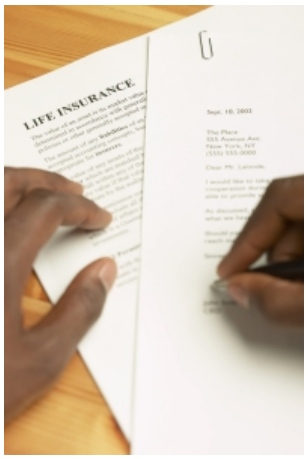
- Transfers may be subject to GSTT and/or gift tax
- Trust document must include a Crummey withdrawal provision if you want to qualify for the present interest gift tax exclusion
- Beneficiaries may have to include lapsed gifts in taxable estate
- You lose control of your assets
- May be costly (trusts incur up-front costs and often have ongoing administrative fees)

Variations from state to state

- In community property states, couples owning community property and who qualify can give $30,000 (in 2020 and 2021) per beneficiary under the present interest exclusion for gift tax without electing gift-splitting. Couples in common law states must affirmatively elect to split gifts.

How is it implemented?

- Contact your insurance agent
- Hire an attorney
- Choose your beneficiaries
- Select a trustee
- Fund the trust
- Serve proper Crummey notice on the beneficiaries
- File gift tax returns, if necessary



Note: Any guarantees associated with payment of death benefits, income options, or rates of return are subject to the claims-paying ability and financial strength of the insurer. Policy loans and withdrawals will reduce the policy's cash value and death benefit and may cause the policy to lapse. Withdrawals may be subject to surrender charges and income tax, and a 10% penalty may apply to withdrawals from a modified endowment contract if made under age 59½.

Note: Variable life and variable universal life insurance policies are offered by prospectus, which you can obtain from your financial professional or the insurance company. The prospectus contains detailed information about investment objectives, risks, charges, and expenses. You should read the prospectus and consider this information carefully before purchasing a variable life or variable universal life insurance policy.

[1] Death benefit is only guaranteed as long as premiums are paid to keep the policy in force.

[2] Dividends are not guaranteed.

Comparison of Types of Life Insurance

	Term	Whole Life	Universal Life	Variable Life	Variable Universal Life
Premium	Premiums increase at each renewal	Level	Flexible	Level	Flexible
Coverage	Usually renewable until at least age 70; for some policies, up to age 95	For life	For life	For life	For life
Death benefit	Guaranteed[1]	Guaranteed[1]	May be guaranteed, depending on policy[1]	Guaranteed[1]	May be guaranteed, depending on policy[1]
		May increase with dividends[2]	Can be increased or decreased	Varies relative to cash value investment returns	Can be increased or decreased; varies relative to cash value investment returns
Cash value	None	Guaranteed	Guaranteed minimum interest rate	Not guaranteed	Not guaranteed
		May increase with dividends[2]	Varies based on interest rates	Fluctuates with subaccount performance	Fluctuates with subaccount performance
Policy loans allowed?	Not applicable	Yes	Yes	Yes	Yes
		May be able to borrow up to 100% of total cash surrender value less annual loan interest rate	Same as whole life, but usually available at lower net interest rate (i.e., pay the interest rate and get a credit back to the policy)	Same as whole life, but usually available at lower net interest rate (i.e., pay the interest rate and get a credit back to the policy)	Same as whole life, but usually available at lower net interest rate (i.e., pay the interest rate and get a credit back to the policy)
Cash withdrawals allowed?	Not applicable	No	Yes	No	Yes
Cash value account growth	No cash value account	Insurer determines guaranteed cash value and declares dividends based on performance of its general investment portfolio[2]	Insurer determines cash value interest crediting rates based on current interest rate returns to the company	Cash value account growth depends upon the investment performance of the subaccounts you choose	Cash value account growth depends upon the investment performance of the subaccounts you choose

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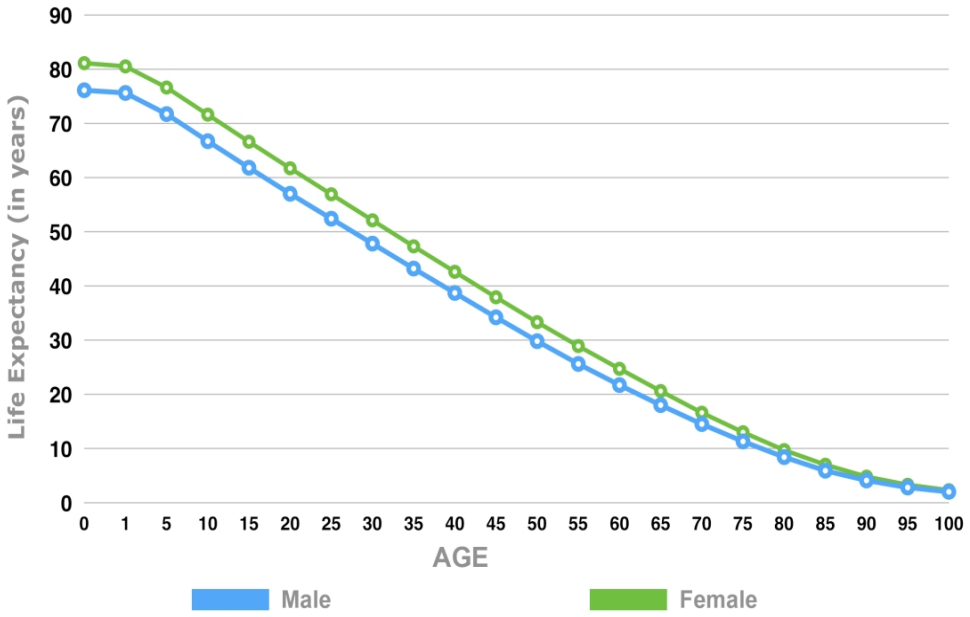
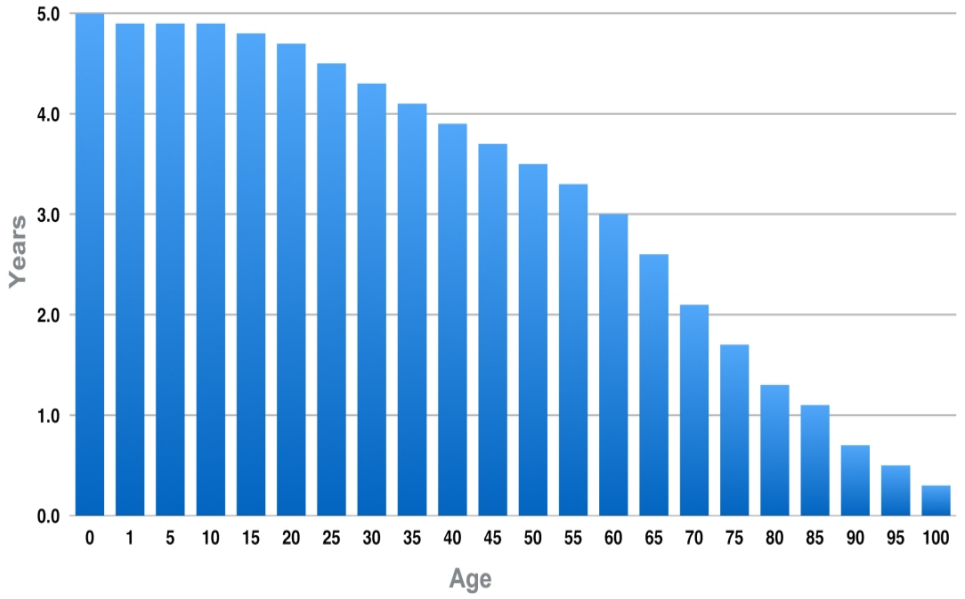
Comparison of Men's and Women's Life Expectancy and Mortality

When it comes to life and death, men and women are not created equal. Couples should take this into consideration when evaluating the need for life insurance. The following charts illustrate the differences between male and female life expectancy and death rates (U.S. population). Source: *National Vital Statistics Report,* Volume 67, Number 5, July 26, 2018.

Life Expectancy: Male vs. Female



Number of Years By Which Female Life Expectancy Exceeds Male Life Expectancy



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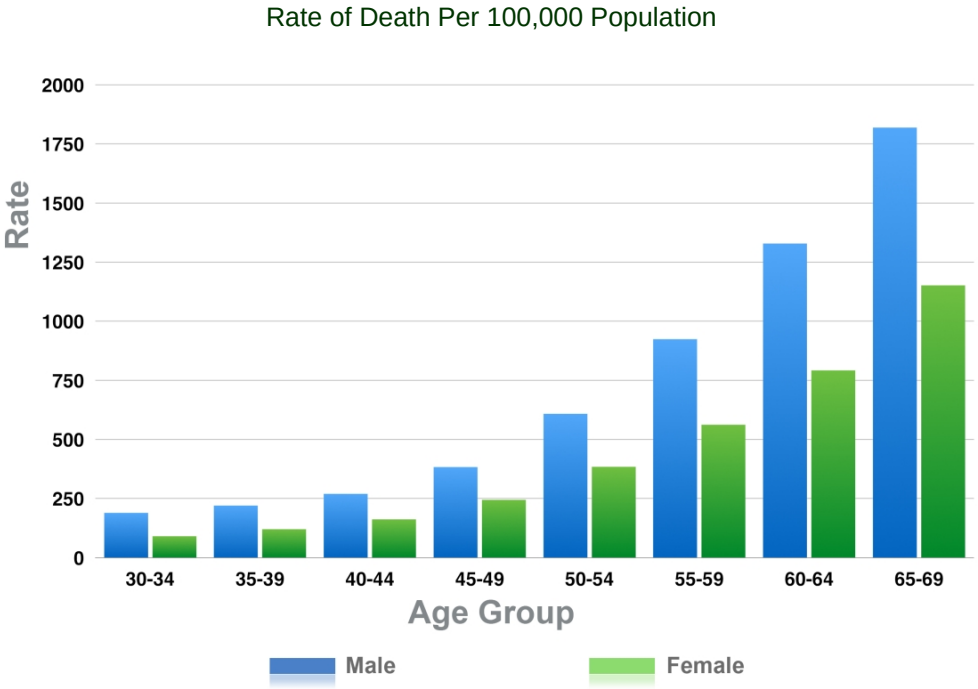
Rate of Death Per 100,000 Population
Rate
2000
1750
1500
1250
1000
750
500
250
0
30-34
35-39
40-44
45-49
50-54
55-59
60-64
65-69
Age Group
Male
Female

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