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Asset Rich, but Cash Poor?

The Solution Might be Financed Life Insurance

by Jeff Verdon, Managing Partner, Jeffrey M. Verdon Law Group LLP

Paul and Shirley, ages 62 and 60, live very simply. They both drive ten-year-old vehicles, clip coupons, and do their own handiwork around the house because hiring a handyman is "too darn expensive." Close friends call them frugal, but Paul and Shirley jokingly say they are just "cash poor." No one would ever guess that Paul's real estate investment portfolio of apartments and mobile home parks has exploded in value since the Great Recession, raising the couple's net worth to almost $30M. Paul and Shirley live on a budget because their investments in real estate are illiquid, making them asset rich, but cash poor, indeed.

When Paul and Shirley met with us to review their outdated estate planning documents, they expressed deep concern over the death tax. Their primary fear was their children being forced to sell "golden" real estate because their estate would have insufficient cash to cover death taxes.

Jeff Verdon

As an estate planning lawyer representing affluent families and successful business owners for more than 30 years, this is a common conundrum faced by many wealthy families. Most have no plan to make cash available to pay death taxes, and heirs often have to sell off assets to raise funds, usually resulting in deeply discounted "fire sale" prices.

Paul and Shirley want their kids to benefit from income generating investment properties long-term, rather than having to make hard choices to sell them off, so I suggested they purchase a last to die life insurance policy. Last to die life insurance policies provide benefits to heirs only after the last surviving spouse dies. Although the couple saw the wisdom of setting up such a sinking fund to pay for death taxes, they couldn't afford its large premium payments. I told the couple that most of my clients don't mind getting life insurance, they just hate paying for it.

"So," I suggested, "Why don't you finance your premiums?"

They both looked at each other and then me, and said in unison, "What is that?"

Financing insurance works like this: instead of writing large annual premium payments to an insurance company, Paul and Shirley would take out a loan to finance the insurance policy and then pay their lender the loan's annual interest. When they both die, if the loan is not yet repaid, the insurance company would write two checks: one to their lender to repay the loan and one to the beneficiary of the policy. The difference in outlay between conventional premium payments versus financed life insurance premiums can be a discount of as much as 65% or more. This keeps funds in portfolios or businesses, where the return on investment will likely far exceed the cost of annual interest on an insurance premium loan.

Paul and Shirley left my office chuckling about being frugal in their asset rich, but cash poor lives… if their friends only knew. Still, such frugality just saved their estate tons of money, and their kids will never experience the heartache of having to sell lucrative, income-generating assets their parents worked so hard to acquire. No hard choices here for anyone.

If you currently have an estate in excess of $5M (if single) or $10M (if married) and have not purchased a life insurance policy to pay your projected death taxes, you may be a candidate for a premium financed life insurance program. Contact the law firm if you would like a complimentary phone consultation about this or any related subject.

For more information, contact Jeff Verdon at 949.333.8150 or jeff@jmvlaw.com.