ADVANCED MARKETS

Insurance planning opportunities in light of new tax laws

The following table highlights key changes to the tax code under the Tax Cuts and Jobs Act of 2017 and life insurance opportunities associated therewith.

KEY CHANGES	LIFE INSURANCE OPPORTUNITIES
Business taxes	
Reduction in top corporate tax rate from 35% to 21%. **Repeal of the corporate alternative minimum tax (AMT).**	When corporate tax rates are lower than individual income tax rates (21% versus 35%), more capital will be retained inside the business. • Increase in key person coverage, including cash accumulation designs, on business owners and non-owner employees • Possible increase in loan regime split dollar and endorsement split dollar as owners focus on designs that retain capital • Increase in non-qualified deferred compensation (NQDC) plans: both SERPs and elective deferral plans • Increased focus on accumulated earnings tax (and legitimate reasons for retaining capital) – Key person coverage is a permissible purpose – Informally funding NQDC is a permissible purpose • AMT repeal removes a potential disadvantage of corporations owning life insurance; might see more redemption buy-sell and corporate-owned life insurance to fund these liabilities
Deduction up to 20% of pass-through income for business owners (subject to strict rules and testing requirements) – may not be available for service oriented pass-throughs like physician's groups, law firms, etc. **Applies to S corporations, partnerships and LLCs taxed as partnerships.**	Deductions available may be heavily dependent on total wages paid to employees – higher wages may mean bigger deductions on pass-through income. • Opportunity for 162 Bonus plans – employee benefit that creates more ties to company than just cash bonuses Service pass-throughs may choose to split their businesses into two entities, with one entity owning the real estate and operating any portions of the business not subject to the personal service limitations. • This may lead to an increase in cross purchase arrangements and the cross endorsement buy sell strategy (since multiple business entities are involved with common owners)
Individual income taxes	
Reduction in top individual tax bracket from 39.6% to 37%. **Doubling the standard deduction; eliminates or reduces many itemized deductions** (e.g., deduction for property taxes and/or state/local income taxes limited to $10,000).	For clients who will see reduced income taxes due to lower rates and/or doubling of standard deduction: • Increased cash flow to help families purchase life insurance (term and permanent sales) and long-term care protection via an LTC rider Taxpayers who currently itemize deductions may see increased or neutral tax impact from tax reform: • Interest, dividends, and capital gain income subject to tax at both the federal and state level, plus exposure to 3.8% net investment income tax, means greater client interest in tax advantages of life insurance (e.g., LIRP and Backstop designs)

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KEY CHANGES	LIFE INSURANCE OPPORTUNITIES
Transfer taxes	
Gift, Estate and GST exemptions increased per individual from \$5M (indexed for inflation) to \$10M (indexed for inflation). **40% tax on transfers exceeding exemption amounts.** **Law "sunsets" to current law after 2025.**	Increase focus on benefits of life insurance beyond federal estate taxes: • Liquidity needs, diversification and IRR analysis, creditor protection, estate equalization, income tax advantages, offset income taxes on assets that don't receive a step-up (e.g., IRA/401(k) assets, assets held in irrevocable trusts), riders for long-term care protection, legacy to heirs and "protective" inheritances • Estate tax exposure still exists: – Number of states with estate and inheritance taxes with much lower exemptions – No change in tax exposure for non-resident aliens (NRAs) with US situs assets (e.g., NRAs only have 13,000 exemption) – Ultra-affluent still have significant estate tax exposure to extent estate exceeds exemptions – After 8 years, law expires and reverts to \$5M exemption (indexed for inflation) • Helping clients meet long-term estate planning objectives before law expires/sunsets: – Individuals have greater opportunity to accomplish wealth transfer to ILITs and dynasty trusts via gifts prior to exemptions reducing to current levels – With new higher exemption potentially going to a lower exemption in 2026, if client doesn't use full exemption during this time, they may lose it – For those on the fence, private financing/split dollar may be way to initiate planning and take a wait and see approach • Generation Skipping Tax (GST) planning: – Apply increased exemption to old trusts that might not have had proper allocation of GST in the past – Decant old trusts (where applicable) into dynastic trusts and use increased GST exemption to allocate to current trust values to make entire trust have zero inclusion ratio – Long-term wealth transfer in trusts leveraged further with life insurance on senior or junior generations

Want to be the first to know about new insurance opportunities and how tax reform impacts various strategies? Visit our new Advanced Market Blog on JHSalesHub.