Preparing for Your Retirement: The Role of Life Insurance in Retirement Planning

Did you know that cash value life insurance is the only financial product with the flexibility to provide benefits if you die, if you become disabled or if you live to retirement?

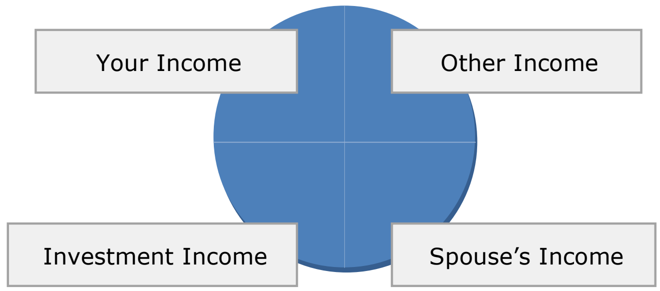
Table of Contents **Page**

Your Earning Power

Your earning power – *your ability to earn an income* – is your most valuable asset.

Few people realize that a 30-year-old couple will earn 3.5 million dollars by age 65 if their total family income averages $100,000 for their entire careers, without any raises.

Earning Power:



How Much Will You Earn in a Lifetime?

Years to Age 65	Your Future Earning Power If Your Family Income Averages:			
	$50,000	**$100,000**	**$250,000**	**$500,000**
40	$2,000,000	$4,000,000	$10,000,000	$20,000,000
35	1,750,000	3,500,000	8,750,000	17,500,000
30	1,500,000	3,000,000	7,500,000	15,000,000
25	1,250,000	2,500,000	6,250,000	12,500,000
20	1,000,000	2,000,000	5,000,000	10,000,000
15	750,000	1,500,000	3,750,000	7,500,000
10	500,000	1,000,000	2,500,000	5,000,000
5	250,000	500,000	1,250,000	2,500,000

If something happens to you during your working years, how will your family replace your earning power?
If, as is likely, you live to retirement, will you have sufficient retirement income to replace your earning power?

Sources of Retirement Income

When you retire and your earning power ceases, you will have to depend on three primary sources for your retirement income:

Social Security

According to the Social Security Administration, the average retired worker in 2021 receives an estimated $1,543 monthly benefit, about 40% of average pre-retirement income. As pre-retirement income increases, however, the percentage replaced by Social Security declines.

Employer-Sponsored Plans and IRAs

You may be eligible to participate in a retirement plan established by your employer and receive pension income at your retirement. You may also be able to contribute to an individual retirement account (IRA) to supplement Social Security and pension benefits.

Home Ownership and Personal Retirement

For many people, there is a gap between the retirement income they can expect from Social Security and employer-sponsored plans/IRAs and their retirement income objectives. Home equity can be used to bolster retirement security. Personal retirement savings, including bank and brokerage accounts and insurance and annuity contracts, can be used to bridge a retirement income gap.

Of these three primary sources of retirement income, personal retirement savings is the one over which we exercise the most control!

Important Facts about Social Security Retirement Benefits

- **The Social Security Normal Retirement Age, age 66 for those people born between 1943 and 1954, is gradually increasing to age 67 for persons born after 1954.**
- **Early retirement results in a permanent reduction in the Social Security retirement benefit.** For example, the Social Security retirement benefit of a worker born in 1959 who retires early in 2021 at age 62 will be reduced by 29.17%.

- According to the Social Security Administration:
  - The **maximum** Social Security retirement benefit for a worker retiring at full retirement age in 2021 is $3,148 monthly.
  - The **average** Social Security benefit for all retired workers in 2021 is an estimated $1,543.

- **The Social Security spousal retirement benefit is limited to a maximum of 50% of the retired worker's benefit.** The spousal retirement benefit is reduced if the worker retires before his or her normal retirement age.

- How much do you want to rely on a source of retirement income over which you have no control? Consider this quote from a *Time* magazine article titled "Social Insecurity":

  "For government to pay pensions to the advancing tide of baby boomers will almost certainly require stunning benefit reductions or huge tax increases. Most likely both. After years of fiscal and political fecklessness, an explosive conclusion."

  Question: When was this article published?

  Answer: March 12, 1995, although the same statement could easily apply today, in the absence of any reform to the Social Security system.

A Potential Solution for a Lifetime…Cash Value Life Insurance

Cash value life insurance is the only financial product with the flexibility to provide benefits:

If You Die...

Should you die prematurely, the death benefit is available to help replace your earning power. This means that funds are available to provide your family with an income, enable them to remain in their home, help pay for an education for your children...whatever the financial needs that arise at your death, funds will be available to help meet those needs.

If You Become Disabled...

With the waiver of premium benefit, your plan can become self-completing in the event of your disability. This means that if you are sick or hurt and unable to work, policy benefits will remain available just as though you were paying the premiums.

If You Live to Retirement...

Most of us can expect to live to retirement age, at which time cash value life insurance can serve as a source of retirement income, while still maintaining needed life insurance protection.* This means that the same life insurance that protected your family's financial security during your working years can continue to play an important role in helping to provide retirement security.

** Withdrawals and loans will reduce the policy's death benefit and cash value available for use.*

Cash Value Life Insurance and Retirement Planning

Cash value life insurance brightens your financial picture with flexibility, accessibility to cash values, tax-deferred growth and an immediate death benefit.

In addition, there are a number of roles that cash value life insurance can play in your retirement planning:

Source of Retirement Income

At retirement, the cash value available in the policy can be:

- taken in a lump sum by surrendering the policy;
- converted into a guaranteed lifetime income; or
- periodically withdrawn and/or borrowed to supplement your retirement income (withdrawals and loans will reduce the policy's death benefit and cash value available for use).

Retirement Income Protection

At retirement, you can elect the maximum life annuity pension option from your pension plan and use life insurance death benefits to help replace your pension income for your spouse, if you should die first. You and your spouse then enjoy a higher pension income while both of you are alive, with the knowledge that if something should happen to you, your spouse will have a continuing source of retirement income.

Accelerated Death Benefits

Many life insurance companies make it possible for policyholders to collect a portion of a policy's death benefit early, if the policyholder is terminally ill, stricken with a specific catastrophic illness or requires long-term care in a nursing home.

Features of Cash Value Life Insurance

Immediate Death Benefit

During your working years, your family is protected by the life insurance. In the event of your premature death, income-tax-free benefits are paid to your family.

Tax-Deferred Growth

Under current law, the annual growth of the cash value in a cash value life insurance contract is not subject to current income tax.

Flexibility

Certain types of cash value life insurance allow you to increase or decrease your premium payments, or make large, single premium payments.

Access to Cash Values

You can borrow or withdraw life insurance cash values prior to age 59-1/2 without tax penalty.*

Ownership

Since you own the policy, benefits are not affected by changes in employment or by changes in Social Security or employer-provided pensions.

Disability Protection

If you become disabled, the waiver of premium benefit can take over your premium payments for you.

Tax-Advantaged Retirement Income

The cash value in the policy can be converted to a retirement income that is partially or fully free from federal income tax.*

** Withdrawals and loans will reduce the policy's death benefit and cash value available for use.*

Tax Issues Affecting the Role of Cash Value Life Insurance in Retirement Planning

Tax-Deferred Growth

The Tax Court has held that cash values are not constructively received by a taxpayer when he or she could not reach them without surrendering the policy. The necessity of surrendering the policy constituted a substantial limitation or restriction on their receipt (Theodore H. Cohen, 39 TC 1055, acq. 1964-1 CB-4).

FIFO Taxation of Withdrawals

Assuming a single premium or periodic premium life insurance contract satisfies the conditions of the "seven-pay test" of IRC Sec. 7702A(b) (i.e., not a modified endowment contract), living benefits received from the contract are taxed under the "cost recovery rule," regardless of when the contract was entered into or when premiums were paid. This means that such amounts received from the contract are included in gross income only to the extent they exceed the investment in the contract (IRC Sec. 7702).

Policy Loans Are Income Tax Free

Policy loans from life insurance contracts are not treated as distributions, assuming the policy qualifies as life insurance under IRC Sec. 7702 and is not considered a modified endowment contract. Upon policy lapse or surrender, the outstanding loan balance is automatically repaid from policy cash values. This may, however, cause the recognition of taxable income. At death, the death benefit will automatically be reduced by the amount of the outstanding loan, an action that does not cause the recognition of taxable income.

Income-Tax-Free Death Benefit

As a general rule, death benefits are excludable from the beneficiary's gross income (IRC Sec. 101(a)(1)).

Income-Tax-Free Accelerated Death Benefits

Depending on current tax law, receiving an accelerated death benefit disbursement may trigger a "taxable event" for the insured. Consult a tax professional about the possible tax implications of accepting a disbursement of accelerated death benefit funds.

Types of Cash Value Life Insurance

There are four types of cash value life insurance from which you can select a policy that best satisfies your needs and objectives. The primary differences in the types of cash value life insurance fall into three categories:

- fixed or flexible premiums;
- responsibility for investment decisions; and
- benefit guarantees or benefits based on actual investment returns.

Whole Life Insurance	The policyowner pays a fixed, level premium and cash values accumulate at a guaranteed* rate of return. The insurance company promises to pay a guaranteed* death benefit. Policy dividends may be payable.
Universal Life Insurance	The policyowner can increase or decrease premium payments and select from a level or increasing death benefit. Cash value accumulations reflect current interest rates or are tied to a stock market index, such as the S&P 500 Index.
Variable Life Insurance	The policyowner pays a fixed, level premium and selects from a variety of investment options for cash value accumulations. There is generally a minimum guaranteed* death benefit and the potential for higher death benefits, depending on the performance of the investment options selected. There is no minimum guaranteed cash value. Instead, the cash value available depends on the performance of the investment options selected.
Variable Universal Life Insurance	The policyowner can increase or decrease premium payments and select from a variety of investment options for cash value accumulations. If a minimum premium payment schedule is maintained, there may be a minimum guaranteed* death benefit. Cash values are not guaranteed. Instead, the cash value available, as well as the potential for a higher death benefit, depend on the performance of the investment options selected.

* Guarantees are subject to the claims-paying ability of the issuing insurance company.

NOTE: Your licensed financial adviser will discuss with you how specific cash value life insurance products may work for you in your particular situation, including the product's features, benefits, risks, charges and expenses.

Important Information

The information, general principles and conclusions presented in this report are subject to local, state and federal laws and regulations, court cases and any revisions of same. While every care has been taken in the preparation of this report, VSA, L.P. is not engaged in providing legal, accounting, financial or other professional services. This report should not be used as a substitute for the professional advice of an attorney, accountant, or other qualified professional.

Life insurance contracts contain exclusions, limitations, reductions of benefits and terms for keeping them in force. All contract guarantees are based on the claims-paying ability of the issuing insurance company. Consult with your licensed financial representative on how specific life insurance contracts may work for you in your particular situation. Your licensed financial representative will also provide you with costs and complete details about specific life insurance contracts recommended to meet your specific needs and financial objectives.

Before purchasing a variable life insurance policy, carefully consider the contract and the underlying funds' investment objectives, risks, charges and expenses. Both the contract prospectus and the underlying fund prospectuses contain information relating to investment objectives, risks, charges and expenses, as well as other important information. The prospectuses are available from your licensed financial representative or the insurance company. You should read them carefully before purchasing a variable life insurance policy.

U.S. Treasury Circular 230 may require us to advise you that "any tax information provided in this document is not intended or written to be used, and cannot be used, by any taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer. The tax information was written to support the promotion or marketing of the transaction(s) or matter(s) addressed and you should seek advice based on your particular circumstances from an independent tax advisor."