When Whole Life Insurance Makes Sense

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What product will pay 3 percent or more annual interest tax-free on monthly deposits over 20 or so years, self-complete in the event of disability, cover long-term-care expenses and multiply your deposits in the event of your death? With safety and certainty?

The answer, of course, is a whole life insurance policy. Yet Suze Orman screams in a video to “buy term insurance and invest the difference!”

Less than 2 percent of term insurance policies pay off as death claims. And most people don’t invest the difference; they spend it.

For young and lower-income families who cannot afford to invest or buy whole life insurance, term insurance is the only answer to protect loved ones until their income reaches the level needed to do better.

Experience is a good teacher. It has taught us that savings accounts turn out to be “put and take” accounts. We save until we see something we just have to have. Then down goes the bank account balance, and we have to start over.

Not so with a whole life insurance policy; you set up an automatic monthly draft that goes into the insurance company month after month and year after year. That account that is silently building year after year is available for a true emergency or an important opportunity or maybe a college education fund while providing protection — or, as in the case of a friend of mine, can provide the funds to meet payroll and payables when others abscond with cash from a business.

When all the early-year needs are met and we approach retirement, where else can the cash accumulation be structured to be paid out tax-free while retaining meaningful amounts of protection or estate preservation?

Let’s shift to the business arena: Where else can you find a guaranteed buyer for a business for the full present-day value with an escalation clause in the event of your death by depositing into an escrow account 2 percent or 3 percent of the value of the business each year? Yes, the escrow account will be part of the purchase price, but the price will have risen proportionally.

One additional feature: Should you die and your heirs call on the “buyer” to honor payment in full for the business, the heir s also keep the business. Another additional feature: Should you become totally disabled before age 65, you will be relieved of having to make the deposits, but the escrow account will continue to grow as though you made them, and the agreement remains in effect.

However, 20 or 30 years down the road, you’re ready to retire. You are given multiple choices: Sell the business to others and get back all your deposits plus about 3 percent to 4 percent interest; sell the business and stop the deposits but leave the agreement intact for the original price by leaving the escrow account in place (cash value buys a paid-up policy); or give the business to your heirs and exercise either of the other options as to the escrow account.

Let’s say we have two partners or equal stockholders. When one dies, what happens? Death terminates a partnership, and many c omplicated legal problems arise — unless a “funded” buy-sell agreement has been put in place whereby the surviving partner receives the funds and pays them over to the estate (spouse?) of the deceased and receives evidence of full ownership in exchange.

A similar arrangement can apply if they are stockholders. Where does the survivor get the funds? Surely the business should not deplete its working capital to implement the agreement. Solution? Cross-purchase life insurance. Each partner/stockholder buys a policy on the other partners/stockholders.

But let’s say neither partner/stockholder dies before retirement, and they decide to sell, pass on to heirs or close the busi ness. Each insured can buy back his/her own policy for the amount of the cash accumulated in the policy. Death proceeds at death will incur no income taxes.

Jan. 13 marked 60 years for Mayer Smith as estate planner; financial planner; adviser to banks, lawyers and CPAs; and creator of insurance and estate concepts copied by others. Contact him at myfriendmayer@gmail.com or 404-725-4841.