

PREMIUM FINANCE OF LIFE INSURANCE is a solution that allows clients to acquire the insurance benefits they need, without impacting current cash flow and the possible cost of gift tax associated with purchasing insurance. The plan is a fully collateralized form of lending, whereby the borrower, typically an entity such as an LLC or an Irrevocable Life Insurance Trust (“ILIT”), borrows the life insurance premiums necessary to pay for a permanent life insurance policy issued on the life of its grantor, is specifically structured to complement a sophisticated estate plan. The ILIT or LLC is the sole responsible party for the premium finance loan, which, from the lender’s perspective removes any credit and bankruptcy risk on the insured. From the insured’s perspective, the loan does not impede his or her borrowing capacity. The loan will be collateralized by a combination of the policy’s cash surrender value and, if and when necessary, additional collateral in the form of cash, marketable securities or a letter of credit, posted on behalf of the ILIT.

The primary reasons for the insured to enter into a premium finance transaction instead of paying cash for the policy are: (a) it allows current investments and cash flow to remain intact; (b) to optimize estate planning and succession planning; and (c) to reduce and in some cases to eliminate the gift tax liability that can be created when using current cash flow for life insurance. In some cases the cash surrender value of the policy may be used for supplemental retirement income.

Successful execution of this transaction requires proper long-term management of both the financing component and the insurance policy itself. The objective of the structure is to provide the client with a lifetime solution, where the premium loan will be repaid from policy cash values or from the proceeds at the client’s passing. Long-term success requires a collaborative effort between the firm designing, underwriting, implementing and managing the solution for the client: the insurance company issuing the policy, and the lender making the loan. The flow chart below depicts the transaction.

