U.S.News & WORLD REPORT

ALSO PUBLISHED IN... YAHOO! FINANCE

HOW TO USE LIFE INSURANCE FOR INVESTING

Investors should start by researching the details and choices.

By: Dawn Reiss - March 15, 2017

Finding the right insurance to invest in – or use for long-term planning – can be complicated for many investors.

Similar to an auto policy, a term life insurance is a temporary policy many individuals use to cover themselves for a period of time and then it expires. Typically it has a lower premium and considered more affordable than permanent life insurance. Many are convertible where the initial plan can be renewed for a higher premium for another term plan or converted into whole insurance.

There are several types of permanent life insurance but all cover individuals for the rest of their lives and include a cash value component.

Whole life insurance has steady, more expensive premiums than term insurance since it lasts a lifetime and includes fixed death benefits and guaranteed cash value accumulation.

Universal life insurance typically offers flexible premiums, an adjustable death benefit and a savings component depending on risk tolerance and asset allocation, but may include a medical exam to qualify. In both cases taxes are deferred and investors can borrow against the cash value of the policy.

Managers suggest options. "Most investors really should not think about insurance as an investment," says Justin Kumar, senior portfolio manager at Arlington Capital Management in Arlington Heights, Illinois. "A whole life insurance policy is a plan to protect more than to invest, and the investment options available in the plan are severely limited. Money is promised as premium for a certain amount of coverage/death benefit, and many investors would be wise to ask a professional for a projection of how that premium money could otherwise be invested."

Kumar says it may make more sense to pay a lower premium to protect with term life insurance and invest what would have been the whole life premium into other accounts that are intended to build wealth. "If an investor's intention is wealth transfer, then a whole life policy could make sense for tax and estate planning purposes," he says.

Either way, investors should consult a tax advisor and estate planning attorney along with their wealth manager so that all parties can give relevant advice and work together, Kumar says.

"Insurance as an investment is not for those folks that need insurance coverage such as new parents or recent homeowners," says Pedro Silva, a financial advisor at Provo Financial Services in Shrewsbury, Massachusetts. "It is best for those folks who need an additional place to invest after they have filled up all other avenues."

Silva says the tax treatment that attracts many people to using life insurance as an investment can also be achieved with a Roth individual retirement account, with much less cost.

If you're considering investing in insurance, Silva says you should already have a cash reserve – typically at least six months of savings within an emergency fund – be taking advantage of any company match on 401(k) contributions, have eliminated all consumer debt and still have discretionary funds to invest.

"It is only at that point that using life insurance as an investment starts to make sense," Silva says. "Between the cost of insurance, the premium fees and modest return expectations, life insurance should be one of the last sleeves of an investment portfolio and, for the most part, will be done by wealthier and clients who can afford to put significant funds into a policy for a number of years."

What to consider before investing. Galen Bargerstock, founder of Government and Civil Employee Services in Lucerne Mines, Pennsylvania, says investors who are considering using life insurance as a vehicle for investing should lean toward a universal policy that offers permanent coverage as a place to invest extra capital.

"Benefits could include things like fixed rates of return and the ability to pull money out of the policy prior to age 59.5 without a tax penalty," Bargerstock says.

It's crucial that investors are aware that there are still life insurance policies available that have fluctuating rates and returns, Bargerstock says. "So it's still important to consider a risk analysis prior to investing," he says.

Bargerstock's advice: conservative investors should look for policies that have a fixed or indexed investment account inside the policy.

"You should consider purchasing a single premium whole life insurance policy if you're looking for somewhere to put your extra cash that will benefit you, in the case you need it," he says.

But term insurance still has its place. "Don't just consider investing in whole life insurance," Bargerstock says. "Term life insurance could be a good investment for someone who is living on a lot of credit and has a lot of significant financial commitments, but still a high income to work with."

Using life insurance as a wrapper. Some industry experts warn against using post-tax dollars in a life insurance wrapped investment – sometimes called a wrapper – since hidden fees and charges may leave investors unaware of how much they could potentially be paying and defeat a potential tax benefit. That's why Richard Myerson, president and CEO of The Myerson Agency, an insurance and retirement firm in Los Angeles, says it's important to know how the wrapper is structured.

"In order to take advantage of the built-in tax efficiency of a life insurance accumulation strategy, the policy must be engineered such that it meets certain IRS-imposed tests to ensure it is not deemed a modified endowment contract," Myerson says. "If a policy fails these tests and is deemed a MEC, much of the tax benefit would be lost."

Myerson says careful advanced consideration must be given to the size and number of annual deposits.

Investors should also understand this long-term investment is illiquid in the early years of funding.

"While the policy-owner can surrender the contract at any time, with many contracts, there will be severe penalties in the form of surrender charges in the early years," Myerson says. "These surrender charges will be reduced over the term of the contract and will usually be eliminated over 10 to 15 years, depending on the product being used."

Investors should acquire an insurance product that is consistent with their long-term objectives, since there are various levels of risk and exit flexibility, Myerson says.

Galen Bargerstock, president of Government & Civil Employee Services, LLC (GCES), is concentrated on navigating federal and state employees through financial and retirement planning. Galen holds a Pennsylvania Life, Health and Annuity License, as well as Series 6 and 63 licenses.

To contact Galen, call 800-985-3272 or visit gces.us.