



WealthPlanningNetwork™

Managing Wealth Across Family Generations

Harness the Power:
Private Placement
Life Insurance and
Variable Annuities

Maximize wealth and enhance after-tax returns
for affluent individuals and families

Maximize wealth and enhance after-tax returns for **Affluent Individuals and Families**

Wealthy investors have unique challenges compared to other types of investors. Affluent clients have a fundamental investment objective:

Grow wealth tax-efficiently across generations while investing flexibly across traditional and alternative investments.

Wealthy Investors should consider two powerful wealth enhancement and tax mitigation tools. These time-tested structures can enhance the compounding of wealth by relieving the tax friction that erodes returns:



Private Placement Life Insurance (PPLI)



Private Placement Variable Annuities (PPVA)

Who Can Invest in Private Placement Life Insurance and Variable Annuities?

PPLI and PPVA investors must meet SEC Accredited Investor (\$1 million net worth) and Qualified Purchaser (\$5 million investments) standards to invest. In addition, investors must have sufficient liquidity to invest the minimum amounts required by insurance companies.

Minimum Investment

PPLI
\$1 million

PPVA
\$500 thousand

Meeting the Tax Challenge for the Affluent

It's not what you earn, it's what you keep that matters."

Investors face a heavy potential tax burden. Federal taxes on investment income and gains can significantly reduce after-tax returns.

2023 Federal Tax Rates For Investors*

40.8%

Ordinary Income
*Includes 3.8% Medicare tax

23.8%

Capital Gains

23.8%

Dividends

The combined impact of federal and local taxes can further reduce returns for investors in high tax regions. The tax burden can significantly reduce after-tax returns on alternative investments and other less tax-efficient strategies.

HEAVY TAXES ON TAXABLE INVESTMENTS CAN CUT RETURNS IN HALF

	Impact of Taxes on 10% Pre-Tax Return			Pre-Tax Return	Net After-Tax Return
	Federal Tax Rate at 36.55%	State and Local Tax	Deduction for State and Local Tax		
Federal Tax	-3.66%	0.00%	0.00%	10.0%	6.35%
Chicago, IL	-3.66%	-0.70%	0.00%	10.0%	5.65%
New York, NY	-3.66%	-1.27%	0.00%	10.0%	5.08%
San Francisco, CA	-3.66%	-1.33%	0.00%	10.0%	5.02%

For illustration only.
Not an actual investment.
Source: Winged Keel

Assumptions:

- Returns include 25% long-term gains and 75% short-term gains or ordinary income
- 23.8% federal tax rate on long-term gains and a 40.8% federal tax rate on short-term gains and ordinary income
- Combined state and local taxes of 5.00% for Chicago, IL; 12.70% for New York, NY; and 13.30% for San Francisco, CA
- State and local taxes are non-deductible due to the \$10,000 limitation

A Potential Solution

Private placement life insurance and variable annuities can provide a way for affluent investors to mitigate the tax burden on their investments and increase after-tax returns. Advisors can utilize these vehicles to achieve "tax alpha" and enhance results for their clients. This guide seeks to provide an introduction to these time-tested tools.

What is "Tax Alpha"?

Tax alpha is the potential value and enhanced returns created by effective tax management when investing.

Source: Morgan Stanley



WHICH IS RIGHT FOR AFFLUENT INVESTORS: PPLI OR PPVA?

What are Private Placement Variable Life Insurance and Annuities?

PPLI and PPVA are insurance solutions for wealthy investors that enhance the after-tax returns of alternative strategies and other investments that may generate substantial taxable income.

Key Similarities and Differences: PPLI vs. PPVA



PPLI Private Placement Life Insurance

Contract with a financial institution to provide a death benefit to beneficiaries



PPVA Private Placement Variable Annuities

Contract with a financial institution to provide a future income stream

- | | |
|--|---|
| <ul style="list-style-type: none">✓ Income-tax-free death benefit✓ Withdrawals or loans generally not subject to income tax (based on policy structure)✓ Mitigate estate taxes by owning PPLI in an irrevocable trust✓ Life insurance required✓ Key tax regulation: Internal Revenue Code Sections 101 and 7702 | <ul style="list-style-type: none">✓ Tax-deferred compounding✓ Withdrawal of earnings or pre-tax contributions are taxed as ordinary income (plus 10% excise tax for withdrawals before age 59½)✓ Withdrawals for supplemental income (annuitization of PPVA is rare)✓ No life insurance required✓ Key tax regulation: Internal Revenue Code Section 72 |
|--|---|

Lower costs and institutional pricing vs. retail insurance products

Institutional pricing maximizes compounding

Reallocate within PPVA or PPLI without triggering taxable gains

No K-1s

Which is right for the **Affluent Investor**?

PPLI and PPVA are both offered by insurance companies. Qualified purchasers can use PPLI and PPVA to meet specific objectives, as illustrated below.

	PPLI	PPVA
Investment Goals		
Invest without current tax liability to enhance compound returns	✓	✓
Optimize returns of alternative strategies and other tax-inefficient investments through tax-deferral	✓	✓
Guaranteed lifetime income option		✓
Tax Considerations		
Defer taxes on investments	✓	✓
Eliminate income taxes on investments at death of insured	✓	Charitable Request only
Liquidity Planning		
Withdrawals of after-tax contributions not subject to tax; gains subject to ordinary income tax (plus 10% excise tax before age 59 ½)		✓
Withdrawals not subject to tax up to amount of premiums paid; gains subject to ordinary income tax upon policy surrender	✓	
Access 80% to 85% of account value through low-cost loans (depending on policy structure)	✓	
Legacy and Estate Planning		
Leave a legacy to children or family	✓	
Intergenerational wealth transfer	✓	
Leave a legacy to a charity	✓	✓
Provide a legacy, but be able to access assets while you're alive	✓	✓
Optimize after-tax performance of trust assets	✓	
Help heirs avoid selling assets to meet estate tax liabilities	✓	



THE POWER OF TAX-DEFERRED COMPOUNDING WITH PRIVATE PLACEMENT VARIABLE ANNUITIES

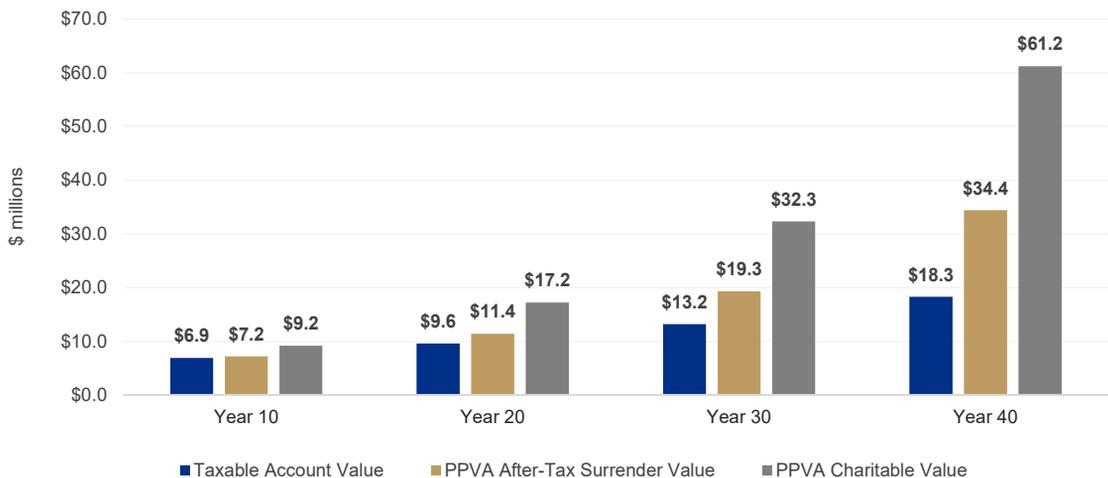
The Power of PPVA vs. Taxable Investing

Investors first discover the power of tax-deferred investing through retirement accounts. However, contributions to retirement accounts are capped. Private Placement Variable Annuities allow for unlimited contributions and tax-deferred accumulation.

The chart below illustrates the power of tax-deferred compounding in a Private Placement Variable Annuity. Over a 40-year period, investors can nearly double their after-tax value through tax-deferred compounding. Investors can more than triple their after-tax capital if they bequest their assets to a charity or family foundation.

PPVA can enhance capital accumulation through tax deferral

PPVA vs. Taxable account: hypothetical growth of \$5 million with 7% net annual return



Source: Winged Keel

Hypothetical illustration only. Not actual results. Not indicative of the performance of any investment. PPVA returns will vary and you may receive more or less than the amount invested.

Assumptions:

- Hypothetical Illinois resident with \$25 million net worth
- \$5 million initial contribution
- 7.00% net rate of return
- M&E expenses:
 - 65 basis points <\$10 million
 - 55 basis points \$10-\$20 million
 - 45 basis points \$20-40 million
 - 37 basis points \$40+ million
- Based on 2023 maximum marginal tax rates:
 - 37.00% federal income tax
 - 20.00% long-term capital gains tax
 - 3.80% Medicare surtax
 - 5.00% Illinois income tax
- Assumes 47.79% combined tax rate for short-term capital gains and ordinary income, and 30.79% combined tax rate for long-term capital gains



THE POWER OF TAX DEFERRAL AND MITIGATION WITH PRIVATE LIFE INSURANCE

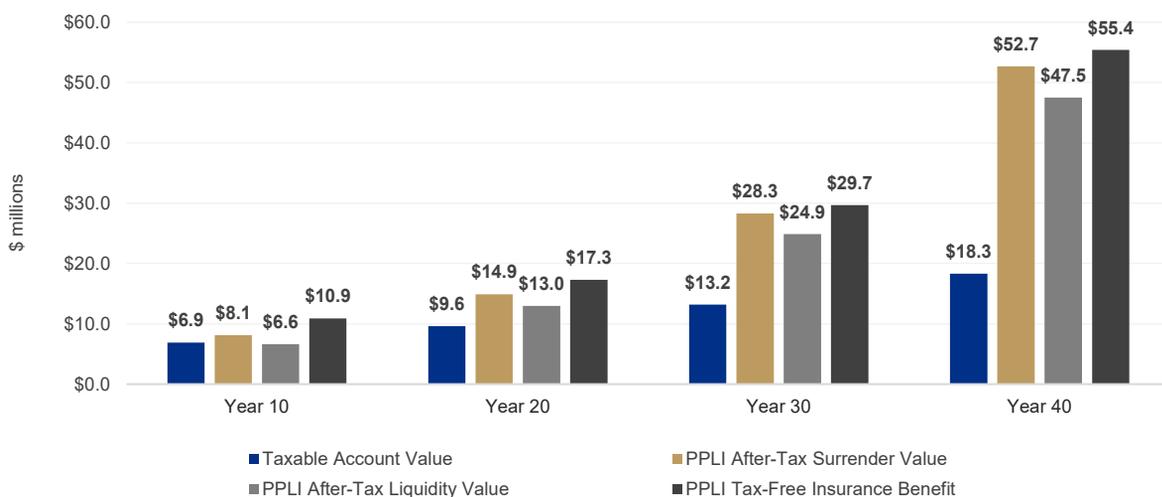
The Power of PPLI vs. Taxable Investing

In addition to offering enhanced after-tax returns, PPLI provides an insurance benefit for beneficiaries that is not subject to income tax. Moreover, owning PPLI within a properly structured irrevocable trust can mitigate estate taxes.

The chart below illustrates the power of tax-deferred compounding in a Private Placement Life Insurance policy. Over a 40-year period, investors can triple their after-tax legacy to beneficiaries.

PPLI can enhance the value of a legacy through tax deferral and mitigation

PPLI vs. Taxable Account: Hypothetical Growth of \$5 Million with 7% Net Annual Return



Source: Winged Keel

Hypothetical illustration only. Not actual results. Not indicative of the performance of any investment. PPVA returns will vary and you may receive more or less than the amount invested.

Assumptions:

- Hypothetical Illinois resident with \$50 million net worth
- Funding of \$1.25 million per year for 4 years
- 7.00% net rate of return
- M&E expense: years 1-20 = 55 bps; years 21+ = 30 bps
- Cost of insurance assumes preferred health rating
- Based on 2023 maximum marginal tax rates:
 - 37.00% federal income tax
 - 20.00% long-term capital gains tax
 - 3.80% Medicare surtax
 - 5.00% Illinois income tax
- Assumes 47.79% combined tax rate for short-term capital gains and ordinary income, and 30.79% combined tax rate for long-term capital gains

PPVA Overview and Highlights



Primary Tax Advantages

- Tax-deferred investing
- Reallocate without incurring taxes



Contributions

- No limit on amounts or timing of contributions



Underwriting

- No medical underwriting



Transfer or Surrender

- No surrender charges
- Tax-free exchanges from expensive retail annuities to a new PPVA per Section 1035 of the Internal Revenue Code



Pricing

- Clear, transparent, institutional pricing for annuity and investments
- Lower fees than retail variable annuities
- No life insurance premiums, loads, or ongoing cost of insurance



Tax Reporting

- No K-1s



Taxation

- Income and gains within PPVA are tax-deferred
- Deferred gains and earnings are subject to income tax at ordinary rates upon withdrawal
- 10% excise tax on earnings if withdrawn before age 59½
- Ability to bequeath an annuity tax free to charity or family foundation
- For systematic withdrawals, a portion of each distribution is considered a return of capital and not subject to tax



Annuitization

- PPVA investors generally utilize elective withdrawals for supplemental income
- Option to receive guaranteed lifetime income by annuitizing (infrequent for PPVA)



Withdrawals

- No contractual limitations on withdrawals
- No Required Minimum Distributions (RMDs), unless annuity is purchased with pre-tax assets
- No distributions required until age 95 (industry standard; may vary by insurance company issuing annuity)



Investment Risk

- Value of policy increases or decreases with performance of underlying investments
- No principal guarantees with low-cost PPVA, as compared to retail variable annuities

PPLI Overview and Highlights



Primary Tax Advantages

- Tax-deferred investing
- Reallocate without incurring taxes
- Insurance benefit not subject to income tax
- Estate tax not applicable to insurance benefit if policy is owned by a properly structured irrevocable life insurance trust (ILIT)



Contributions

- Potentially significant contributions, subject to insurance underwriting
- Potential flexibility in amount and timing of deposits
- Maximum annual contributions determined by IRS guidelines, required life insurance premiums, and insurance market capacity



Underwriting

- Medical: insurers evaluate health status of insured to determine pricing
- Financial: proof of economic need for insurance
- Insurable interest: purpose of policy to protect against economic loss or other hardships



Liquidity

- Potential flexibility to accommodate liquidity needs of policyholder
- Withdrawals up to cost basis not subject to tax
- Properly structured loans may be utilized to access policy cash value to minimize taxation of distributions (for non-Modified Endowment Contracts only)
- Potential to access approximately 80% to 85% of after-tax PPLI account values during insured's lifetime



Transfer or Surrender

- No surrender charges
- Tax-free exchanges from expensive retail life insurance policies to a new PPLI per Section 1035 of the Internal Revenue Code



Pricing

- Clear, transparent, institutional pricing for policy and investments
- Lower fees than retail life insurance
- Potential syndication among insurance companies to optimize pricing and capacity
- Competitive, transparent pricing for Mortality & Expense (M&E) costs



Crossover Point

- Higher insurance premium costs in early years
- Crossover point to overcome early insurance costs is generally 10+ years



Tax Reporting

- No K-1s



Taxation

- Income and gains within PPLI are tax-deferred
- Deferred gains and earnings are subject to income tax at ordinary rates if policy is fully surrendered
- No income tax on insurance benefit
- Estate tax relief if policy is owned by a properly structured irrevocable life insurance trust (ILIT)



Investment Risk

- Value of policy increases or decreases with performance of underlying investments

MEC OR NON-MEC?

A modified endowment contract (MEC) is a cash value life insurance policy that loses a variety tax benefits. If a life insurance policy has too little insurance and too much cash value, policy loans can become subject to income tax. PPLI contracts are carefully structured and require a sufficient insurance component, particularly in the first seven years of a contract, to be considered "non-MEC" contracts and thus retain the significant tax planning benefits of life insurance, including tax-free policy loans.



HARNESS THE POWER: INVESTING WITHIN PPLI AND PPVA

Insurance Dedicated Funds

There are numerous options for investing within PPLI and PPVA. These investment options are structured specifically to meet stringent tax regulations. These funds are called Insurance Dedicated Funds or IDFs.

There are two primary types of IDFs:

- **Registered** IDFs, also called **Variable Insurance Trusts** or **VITs**, which invest mainly in traditional assets, such as stocks and bonds
- **Private** or **unregistered** IDFs, which invest primarily in alternative strategies, including private credit, private equity, hedge funds, trading strategies, and funds of funds

The universe of IDFs is robust, with over 600 investment options, encompassing the spectrum of traditional and alternative investments. Each insurance carrier will offer a curated selection from this universe for their policies or annuities. Investors may allocate and reallocate between IDFs without incurring taxes.

Investment Universe of Insurance-Dedicated Funds

Registered IDFs or VITs Primarily Traditional Assets	Unregistered IDFs Primarily Alternative Strategies
400+ Registered IDFs	200+ Unregistered IDFs
Publicly Registered under the Investment Company Act of 1940	Accredited Investors and Qualified Purchasers Only
Common Investment Options	
Stocks	Private Equity
Bonds	Private Credit
Balanced	Hedge Funds
Multi-Asset	Trading Strategies
Liquid Alternatives	Funds-of-Funds

Separately Managed Accounts

Separately managed accounts represent a growing trend for the largest investors in PPLI and PPVA. With this approach, the insurance company retains an investment manager to supervise a custom segregated insurance company separate account on behalf of the client.

PPLI/PPVA Investment Considerations

For the PPLI and PPVA investments to maintain their tax-favored status, they must comply with two key tax provisions:

1

Investor Control Doctrine

Investing within an insurance structure requires strict adherence to the IRS Investor Control Doctrine to preserve the tax benefits. Under this doctrine, assets must be segregated and under the purview of the insurance company. Thus, insurance company segregated accounts or insurance-dedicated funds (IDFs) are utilized within the life insurance policy or annuity. The policyholder can then select from a menu of compliant investments within their policy or annuity.

In addition, the policyholder must not communicate with or direct the investment manager overseeing the assets. A policyholder may select the manager or the funds, but then must relinquish investment control to the fund manager. The policyholder is still free to change the portfolio of permitted funds within the policy or annuity.

2

Diversification Requirements

Insurance regulations require a diversified approach to investing to preserve eligibility for tax-favored investments. In general, each IDF or insurance company segregated account in a variable life policy or annuity must contain at least five investments with:

No more than

55%

of the account value represented by any **one** investment

No more than

70%

of the account value represented by any **two** investments

No more than

80%

of the account value represented by any **three** investments

No more than

90%

of the account value represented by any **four** investments

These rules, known as 817(h), are requirements for the managers of the investment funds within a policy or annuity, and are not direct requirements for the policyholder.



Investor Protection

Assets held within an insurance company separate account, IDF, or VIT are segregated from insurance company assets and are protected from insurance company creditors.



PUTTING THE POWER TO WORK FOR HIGH-NET- WORTH INVESTORS

Coordinating the Client Team

Developing and implementing the right PPLI or PPVA solution for High-Net-Worth Clients requires a team of specialists. Wealth Planning Network leads the Team of Specialists that work directly with our clients to achieve their unique goals and objectives.



Financial Advisor

- Develop financial plan and recommendations
- Provide comprehensive review and understanding of transaction



Insurance Professional

- Product expertise
- Case design and illustrations to meet client objectives and optimize results
- Guide client through underwriting process
- Develop risk profile and negotiate underwriting with insurance companies
- Prepare applications and place coverage
- Ongoing service for clients and advisors for the life of the contracts



Investment consultant

- Advise on investment choices
- Coordinate insurance with overall investment allocation



Attorney

- Legal and tax expert
- Develop and update estate documents
- Advise on policy ownership structure
- Negotiate with counterparties on client's behalf



Insurance Company

- Underwrite and issue policy
- Provide investment options
- Reinsure excess risk for large policies
- Report policy values to policy owner in partnership with service professionals



Fund and Investment Managers

- Execute investment management agreement with insurance company, IDF, or VIT
- Manage assets
- Certify 817(h) diversification compliance
- Report portfolio or fund values

Source: Giordani, Baker, Grossman & Ripp LLP

Put PPLI and PPVA to work for you



PPLI and PPVA are potentially powerful tools to **enhance after-tax returns** for you. Both can help strengthen your finances over time.



PPLI and PPVA **differ in implementation** and may entail trade-offs.



PPLI provides for **tax-deferred accumulation** of policy values and can be structured to mitigate the impact of income and estate taxes. However, PPLI entails insurance underwriting, medical exams, and the cost of insurance. Policyholders can make significant contributions to PPLI, but annual deposits are **regulated by IRS guidelines** and insurance market capacity.



PPVA can also **increase after-tax returns** for clients. However, income taxes on earnings will be due when withdrawn, unless left to a charity or family foundation. Regardless, PPVA is not subject to insurance underwriting or costs, and **contributions are not limited** by insurance constraints.



Both PPLI and PPVA provide a **wide variety of investment options** through IDFs and VITs. In particular, they enable tax-deferred compounding for investors in alternatives and other investments that may otherwise produce significant taxable income.

Quick Take

Comparing PPLI, PPVA,
and Taxable Investments:



Tax Benefits



**Operational
Benefits**



**Liquidity
Considerations**

	Taxable Investments	PPLI	PPVA
Income Tax Benefits			
Tax Deferral	No	Yes	Yes
Income Tax Elimination	No	Yes, if policy is held to insured's death	Yes, if beneficiary is tax-exempt
Estate Tax Benefits			
Estate Tax Elimination	No	Yes, depending on ownership structure	Yes, if beneficiary is tax-exempt
Exempt From Generation-skipping Tax	No	Yes, depending on ownership structure	No
Estate Planning Applications	No	Yes	Yes
Operational Benefits			
Annual K-1	Required	No K-1	No K-1
Protected From Insurance Company Creditors	n/a	Yes	Yes
Death Benefit	No	Yes	No
Medical Underwriting	No	Yes	No
Liquidity Considerations			
Ability to Borrow Against Policy Cash Value Tax-free	n/a	Yes, depending on policy structure*	No
Ability to Withdraw Principal Tax-free**	n/a	Yes, depending on policy structure*	Yes, for after-tax contributions

*If policy is structured as a non-Modified Endowment Contract (MEC). If policy is structured as a MEC, last-in-first-out (LIFO) taxation applies. All withdrawals of earnings are taxable prior to non-taxable return of principal.

**Withdrawals may be subject to recapture ceiling

Source: Lombard International, RiskBridge Advisors



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Wealth Planning Network has not given any legal or tax advice related to the premium financing arrangement, and assumes no responsibility for the obligations, demands, losses, or liabilities, including attorney fees, resulting from the premium financing arrangement.

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