A Smooth Sailing Approach to Retirement Planning

Life Insurance

sales idea

Managing the effects of financial market fluctuations is a critical element in retirement planning, and financial professionals understand how to develop retirement strategies that help ride out these highs and lows during the accumulation years.

However, once a client moves out of the accumulation phase and into the distribution phase, market highs and lows present a different type of challenge. If retirement distributions begin in a stable or rising market, clients have the potential to preserve or even grow their retirement assets. But if these clients begin distributions in a declining market, they are often drawing down and selling into losses. Their assets may begin to erode faster than initially planned. During the 2008 market crash, people who had originally planned to retire that year found they had to either delay retirement or unexpectedly return to the workforce, often at reduced salaries.

For clients and financial professionals concerned about how to manage this type of risk, cash value life insurance offers a possible solution in protecting clients, both during their working years and in their retirement years.

The Challenge

Tom is 65 and has accumulated $1,000,000 toward his retirement. Like many people today, he knew he had to build a retirement pool of his own. To maintain his current standard of living, he needs $100,000 a year in retirement and there is little coming in to support from other sources:

- **Social Security —** $20,000
- **Pension —** $10,000
- **Tom's Savings —** need to make up the other $70,000

Tom knows he needs to draw from his $1,000,000 retirement fund at $70,000 per year. However, he's concerned that if the stock market is unstable he may not have sufficient funds. He works with his Financial Professional and they look at a 20-year return for the market, until he's 85. They don't look to the 1980s and 1990s, where markets saw increases in most years. Instead, they look to what the market experienced in the 1970s and 1980s, when there was a mix of gains and losses.

Tom's Results without Life Insurance

Starting Balance at Age 65	Annual Retirement Fund Withdrawals Before 1% Inflation	Tom's Retirement Fund Balance at Age 85
$1,000,000	$70,000	$444,791

This is the result Tom might see (assuming the same market returns as in the 1970s and 1980s). This is the result of ONLY five down years over a twenty-year period, and assuming a very low 1% inflation.

By taking funds out of his retirement savings year in and year out, Tom is forced to sell into loss years. In effect, Tom locks in and exacerbates his losses during down market years.

AXA Equitable Life Insurance Company (NY, NY)

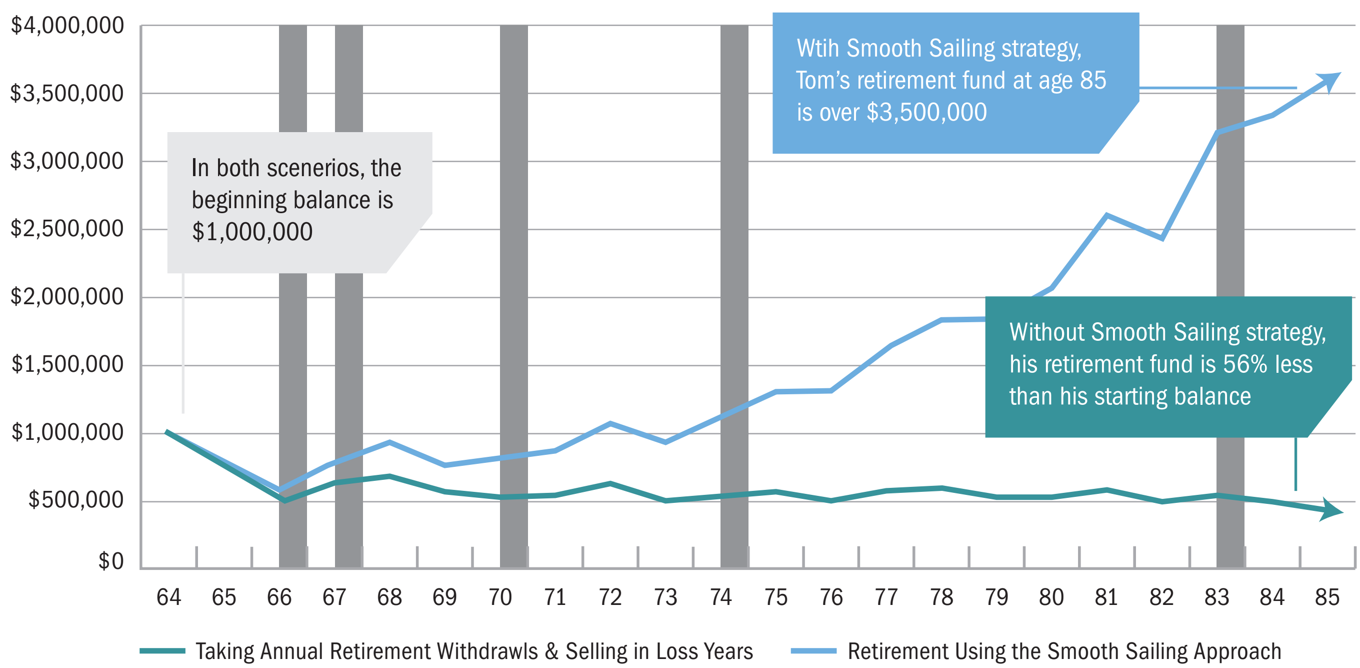
Smooth Sailing — A Possible Strategy with Life Insurance

Tom has one advantage that his Financial Professional brings to his attention. When he was in his 40s, Tom bought a cash value life insurance policy. At the time, the insurance was intended to protect his family if something happened to him during his working years. Now, at age 65, the policy has a reasonable cash surrender value that Tom can access to help supplement his retirement.

His Financial Professional shows Tom a strategy called Smooth Sailing where he can supplement his retirement income in a way that may give him an answer to his retirement challenge. Tom continues to take distributions from his $1,000,000 retirement pool. However, following down market years, Tom could instead access his policy's cash surrender values, and avoid selling into market losses.

The gray bars below represent the five down market years during the 1970s and 1980s, based on the returns of the S&P 500® Price Return Index.. These are the years in which Tom would take a distribution from his life insurance policy instead of his retirement pool.

Table — Title 1



Past performance is not indicative of future results. Clients cannot invest directly in the S&P 500® Index.

As a result, Tom preserves his traditional retirement funds, allowing them time to recover. Adding a cash value life insurance policy to the mix avoids selling in down years and locking in losses. What's more, using life insurance – an asset with different taxation – may enhance Tom's retirement fund and allows him to leave a legacy to his family. Using cash value life insurance in retirement allows Tom to Smooth the Sailing on the uncertain waters of retirement.

How Is Smooth Sailing Different from Traditional Retirement Strategies Using Life Insurance?

Most retirement strategies with cash value life insurance use a maximum-funded policy to maximize the tax advantages offered by life insurance cash value accumulation. In retirement, these maximum funded policies are usually illustrated showing withdrawals and loans over 20 years. However, with the Smooth Sailing method, Tom is making strategic withdrawals only in certain years (the years following down stock markets). As a result, he doesn't need to maximum fund his life insurance policy. He simply needs to adequately fund it to build some cash value. In this example, Tom had a $500,000 policy and he funded it at $7,000/year (about $580/month).

Policy loans and withdrawals will reduce the cash value and death benefit of the policy. The client may need to fund higher premiums in later years to keep the policy from lapsing.

How Life Insurance Benefits Can Help Clients Smooth the Uncertain Waters of Retirement

By purchasing permanent cash value life insurance instead of term insurance, Tom provided for his family in multiple ways:

- He has the death benefit during his working years to protect his family.
- At retirement he has a reasonable cash value that he can tap in retirement, as needed.
- He has an asset with special tax treatment.
- By using the Smooth Sailing approach with life insurance, Tom is also potentially able to provide his family with a legacy by not depleting his assets in retirement.

benefits of the smooth sailing approach

- Clients with life insurance can protect their families against losses in the event of an early death (pre-retirement).
- During retirement, the cash values in a life insurance policy can offer clients a safety net by providing funds that they can draw on to avoid selling into market losses for retirement funds.
- The tax treatment afforded life insurance withdrawals and loans may offer clients other tax advantages when accessing their policy cash values.

target client profile:

- Has a life insurance need,
- Is 35-55 years old,
- Is already funding traditional retirement options (IRAs and 401ks), but has a need for additional funding,
- Is concerned about what will happen to retirement funds in the event of a market drop while he or she is in or approaching retirement age.

Timing Is Everything

Market performance in the earliest years of retirement can make or break a client's long term retirement. Retiring in a down market drove down Tom's retirement assets from $1,000,000 to $444,791, a 56% reduction (and at only 1% inflation). Had he retired in a different market, his results would have been remarkably different. Looking at the market return from 1990 to 2010, his $1,000,000 starting point would have grown to $2,195,599. This time frame included, arguably, one of the market's best decades followed by one of the market's worse decades. Despite the negative and flat returns of the 2000s, the strong performance in the 1990s would have given Tom a strong cushion even a decade into his retirement. The point is, clients never know what they'll face when they retire.

Permanent cash value life insurance helps offer clients multiple protections. Not only does it offer protection for their families during their working year, the cash values offer clients multiple options in retirement. In the Smooth Sailing approach, the cash values allow clients to make selective withdrawals to help avoid selling into market losses.

Even without maximum funding a life insurance policy, the cash value life insurance helps clients meet multiple goals of protection, retirement funding and wealth transfer.

Other Considerations

- If clients are able to actually achieve strong early year returns, they won't have the same risk related to their retirement funds, but they will have a life insurance benefit and its cash values to enhance their overall financial goals. This strategy is intended to address the concerns clients might see if they don't receive strong returns early in retirement, as was the case in much of the 2000s.
- There is usually a surrender charge that will vary by type of policy. These charges usually run 15 years or longer and will affect the available amount clients have to withdraw or borrow from their policy at any given time. There are also cost of insurance and other policy charges that will impact the cash value.
- The strategy presented here is intended to reflect a broad concept, and individual situations will be different. In certain cases, clients will not have complete flexibility with all assets. In many instances, IRA and qualified plan assets will require minimum distributions (RMDs) after age 70½. This will force assets out of retirement funds even in years following market losses. However, where clients retire before age 70, these RMDs won't occur in the early years of retirement.
- Some planners might suggest buying term insurance and investing the difference. However, this approach adds funds to the pool of traditional retirement assets that might otherwise face market drops that the Smooth Sailing approach tries to mitigate.
- How much life insurance clients can purchase and the price they pay will depend on medical and financial underwriting. Your clients' results will vary based on their underwriting offer.
- To make this effective, clients will need a long-term buy-and-hold strategy with a cash value life insurance policy.

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