

## SHOULD YOU EXCHANGE YOUR LIFE INSURANCE?

As we go through the various stages of our lives: maturity, marriage, child rearing, house purchases, business obligations- also come financial obligations to both family and creditors. At some point in time we consider the use of life insurance to see to it that our family is secure and our obligations are met. We meet with the agent, secure our policy, stick it in the draw and pay for it as the bills come in. When was the last time you considered your updated needs, or if the old policies fulfill your current needs?

The insurance industry has seen a number of social and demographic changes occur which have forced corresponding changes in the design and cost of life insurance products. Many long-time policyholders have recognized these developments and have considered acquiring new or different policies to take advantages of these updates and changes. Periodic assessment of your life insurance policies is critical to effective risk management and estate liquidity within your financial plan. Fortunately, there is a tool available to exchange an old policy for a new one and not be saddled with any tax burden.

This popular tool is known as a "Section 1035 Exchange" (after IRC Section 1035) and permits you to exchange an old policy for a new one without having to pay tax at the time of the exchange on any gain that built up in the old policy. Many people refer to this exchange as tax-free, but the gain is really deferred, not forgiven.

Generally, IRS rules allow you to exchange a life insurance policy for a new life insurance policy, or to exchange one annuity policy for another. You cannot exchange an annuity for a life insurance policy, however, and use the tax-deferred provision. The insured or annuitant must be the same under both the old and new policies, yet there is no requirement that the owners be the same after the exchange. Finally, you are permitted to exchange multiple policies without recognizing gain, often used where you have a number of old policies you would like to consolidate them into one new policy.

You should be particularly careful when making a section 1035 exchange if you have outstanding loans on your policy. The IRS recognizes unpaid loans in figuring policy gain. Therefore, you might have to payoff policy loans before processing a 1035 exchange to avoid being taxed, therefore, such an exchange may not always be appropriate just to take advantage of lower costs.

You most likely will be required to provide new evidence of your insurability via a medical exam, usually done at your home at your convenience. If your health has deteriorated since you bought the old policy or you are no longer insurable, the insurance company may decline to allow such an exchange or make it too expensive. Always remember, if the exchange is done correctly, your old policy will be in effect up to the point that your new company accepts you as an insured. You should never, ever, allow your existing policy or plan decline until you have in writing acceptance from the new company. If you haven't review your insurance plan in the past 3 years or have had a material change in your lifestyle, call your agent or financial planner for an up to date evaluation, and look how section 1035 may work for you.

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