
Unlocking the Power of Private Placement Life Insurance for RIAs and Family Offices

Comprehensive Strategies for
Tax-Efficient Growth, Wealth
Transfer, and Asset Protection



☎ 605-415-4454

✉ info@iplins.com

🌐 www.investorspreferred.com

Section 1

Understanding Private Placement Life Insurance

What is Private Placement Life Insurance?

Private Placement Life Insurance (PPLI) is a customizable, institutionally-priced life insurance solution tailored for high-net-worth and ultra-high-net-worth individuals. Unlike standard life insurance, PPLI is specifically designed to offer maximum investment flexibility, significant tax advantages, and enhanced wealth transfer capabilities. It is structured as a variable universal life insurance policy, meaning that the cash value of the policy can be invested in a wide array of assets, often including alternative investments like hedge funds, private equity, and other complex asset classes.

Key features that distinguish PPLI include:

- **Tax Deferral:** Investment growth within a PPLI policy is tax-deferred, allowing for more efficient compounding.
- **Tax-Free Access:** Policyholders can access cash values tax-free through loans or withdrawals.^[1]
- **Estate Tax Efficiency:** The death benefit is paid out tax-free to beneficiaries, making it an effective tool for wealth transfer.
- **Investment Customization:** PPLI policies allow for diverse and sophisticated investment strategies, including access to IDFs and SMAs, which provide control and flexibility unmatched by traditional life insurance products.

^[1] Income tax-free loans available if policy is structured as a non-Modified Endowment Contract. Access to cash values through borrowing or partial surrenders will reduce the policy's cash value and death benefit, increase the chance the policy will lapse, and may result in a tax liability if the policy terminates before the death of the insured.

How PPLI Works

PPLI is a highly flexible insurance product that allows policyholders to contribute premiums into a policy whose cash value grows based on the underlying investments chosen within it. These policies are only available for accredited investors and qualified purchasers due to their customization, cost, and complexity.[2] PPLI is offered by insurance companies through a private placement offering memorandum and is regulated under securities laws, which further aligns it with the needs of UHNW individuals.

When premiums are paid into a PPLI policy, they are invested in insurance-dedicated investment vehicles, such as IDFs and SMAs, (discussed later in this paper). The structure allows for:

- **Tax-Deferred Growth:** The policy cash value can grow tax-deferred as long as the funds remain within the PPLI structure.
- **Asset Protection:** In many jurisdictions, assets held within a PPLI policy are shielded from creditors and legal claims, adding a layer of security for policyholders.

One major difference between PPLI and traditional life insurance policies is that in PPLI, each party to the transaction functions in the role to which they are best suited rather than the life insurance company handling most, or all, functions. For instance, with most retail policies, the insurer accepts and holds the premium in its general account. The retail insurer then makes all the investment decisions about how to invest the premium and how much of the yield to share with the policyholder.

With PPLI, the insurer is able to accept the policyholder's choice of investment manager and custodian to choose how to invest and hold the premium, which becomes the policy's cash value.[3] The PPLI insurer

[2] Private placement products offered by U.S. carriers to U.S. persons are subject to SEC regulations. Each purchaser generally must be a "qualified purchaser" under §2(a)(51) of the Investment Company Act of 1940, 15 USC §80a-2(a)(51), and/or an "accredited investor" under §501(a) of Regulation D of the 1933 Act, 17 CFR §230.501(a). A "qualified purchaser" is an individual or a family-owned business that owns \$5 million or more in investments. An "accredited investor" is anyone who meets one of the below criteria: Individuals who have an income greater than \$200,000 in each of the past two years or whose joint income with a spouse is greater than \$300,000 for those years, and a reasonable expectation of the same income level in the current year.

[3] IRC §817(c). A "separate account" is a separate set of financial statements held by a life insurance company, maintained to report assets and liabilities for particular products that are separated from the insurer's general account. Detailed statutory financial statement data and disclosures regarding the products and assets captured in a separate account can be found in SSAP No. 56—Separate Accounts

continues to provide the life insurance policy structure but, unlike a retail insurer which retains much of the death benefit risk, a PPLI insurer reinsures most of the death benefit risk with major, highly rated reinsurance companies. In other words, because there is a sophisticated policyholder who has access to professional investment management, most of the risk of making sure the policy performs is shifted from the insurer to the policyholder.

Section 2

Investment Vehicles Within PPLI - IDF vs. SMAs

PPLI can permit a variety of investment types, depending on the insurance company offering the policy and the investment strategy chosen by the policyholder.

Some common types of investments that can be held within a PPLI policy include:

- **Equities:** PPLI policyholders can invest in stocks of publicly traded companies or private equity funds.
- **Fixed Income Investments:** These include bonds, fixed-income securities, and other debt instruments.
- **Alternative Investments:** PPLI policies can allow investment in alternative assets such as hedge funds, private equity, real estate, and commodities.
- **Cash and cash equivalents:** PPLI policies can hold cash and cash equivalents such as money market funds.

The Internal Revenue Code ("IRC") lays out the treatment of variable life insurance and annuity contracts in Section 817 and authorizes two types of investments by a variable policy, IDFs and SMAs. RIAs and family offices typically engage fund administrators to form IDFs and SMAs in order to attract PPLI policy investment.

Historically, until the last decade, IDFs were utilized almost exclusively as PPLI policy investments. SMAs have emerged in popularity as RIAs and family offices have come to recognize the tax benefits of PPLI and seek to deploy customized portfolio strategies within policies.

Insurance Dedicated Funds (IDFs)

Structurally, IDFs have a number of important characteristics. An IDF is a private fund that is only open to subscriptions from life insurance companies on behalf of their issued PPLI policies. IDF investment portfolios must meet the Diversification Test for variable contracts as outlined in Treasury Regulations Section 1.817-5 or the policy will not be treated as a life insurance policy or an annuity and all tax benefits will be lost.^[4]

Fund managers are permitted to leverage one of their current taxable strategy offerings in a new IDF offering, as long as the investment decisions of the IDF are made by the advisor of such IDF in their sole and absolute discretion.

In general, the insurance carrier or an independent investment advisor engaged by the carrier will select IDFs for subscription on behalf of the policy. Some insurance carriers allow policy owners to influence the allocation of their policy's investment funds among a predetermined set of carrier-approved IDFs. Other carriers require IDFs to be selected by an independent investment adviser. In all cases, Policy owners may not direct or control the investment activity of an IDF held in their policy.

RIAs will often build their own co-mingled IDFs in order to gain efficiency in allocations across multiple clients and to increase the number of clients that can get access to closed or limited capacity managers.

The setup and ongoing administration of an IDF can vary. A fund manager may establish its own standalone IDF, or utilize a third-party administrator that specializes in IDFs.

Fund managers with multiple existing private funds may find it most efficient to establish a standalone IDF. Other fund managers or RIAs without existing fund administration capabilities or service provider relationships may find the services of a specialist IDF administrator to be their best route to managing investments for PPLI policies.

[4] Diversification requires that no more than 55% of the value of the total assets of the account is represented by any one investment, with increasing thresholds for additional investments: no more than 70% of the value for two investments; no more than 80% of the value for three investments; and, no more than 90% of the value for four investments.

Advantages of IDF include:

- **Diversity and Access to Alternatives:** IDF allow PPLI policyholders to diversify into alternative investments, including private equity and hedge funds, without triggering taxable events on gains or income within the fund.
- **Institutional Pricing:** IDF are typically available at institutional pricing levels, which means lower fees than traditional retail options.
- **Customization for UHNW Clients:** IDF within a PPLI policy can be tailored to suit specific financial goals and risk tolerances, adding a high degree of personalization that appeals to UHNW individuals.

The cost to establish an IDF varies depending on whether a fund utilizes internal or external legal support in developing the legal structure. The industry norm is to engage a cost-effective vendor where set-up fees can be as low as \$36,000.[5]

On-going administration fees for access to the vendor's platform are based on an IDF's assets under management ("AUM") and are commonly in this range:

AUM:

- < \$49,999,999 million is 0.15% per year
- \$50 million to \$149,999,999 million is 0.10% per year
- > \$150 million is 0.05% per year

subject to a minimum fee of \$2,500 per month.[6]

IDF costs do not include sub-advisor fees nor agent compensation. These additional fees are also deducted from a PPLI policy's cash value.

[5] Judas, J. C., & Fontanini, M. (2022, January 20). PPLI Market Report. Retrieved April 19, 2024, from <https://www.lifeinsurancestrategiesgroup.com/pplimarketreport>

[6] Judas, J. C., & Fontanini, M. PPLI Market Report. Retrieved April 19, 2024, from <https://www.lifeinsurancestrategiesgroup.com/pplimarketreport>

Separately Managed Accounts (SMAs)

A SMA allows an independent investment advisor to access the broadest possible range of investments for the policy account, including marketable securities, structured notes, ETFs, hedge funds, private equity and other alternative investment strategies. Structurally, a SMA in a PPLI transaction is no different than a SMA an investor would purchase within their investment portfolio.

However, due to the tax benefits of a PPLI, a SMA composed of highly tax-inefficient investments is commonly held under a policy. SMAs are subject to the same diversification requirements and prohibition against investor control as IDFs.

SMAs in the context of PPLI refer to custom-managed portfolios held directly under the policy rather than as part of a pooled investment fund like an IDF. These accounts are usually set up to allow a policyholder's RIA or family office to directly manage investments, thus providing a high level of control over the asset allocation and strategy.

Advantages of SMAs:

- **Direct Management Control:** Unlike IDFs, SMAs offer the policyholder's advisor direct control over investment decisions. This is especially valuable for clients who have specific mandates or investment philosophies.
- **Tailored Asset Allocation:** SMAs allow for a bespoke approach to asset management within the PPLI structure, enabling a fully customized investment strategy that aligns with a client's overall portfolio.
- **Tax and Estate Efficiency:** Assets within the SMA grow tax-deferred, and any proceeds upon death are distributed tax-free to beneficiaries, providing a seamless transfer of wealth.

AUM:

- < \$49,999,999 million is 0.10% per year
- \$50 million to \$149,999,999 million is 0.08% per year
- > \$150 million is 0.06% per year

subject to a minimum fee of \$2,500 per month.[7]

Pricing is generally “program-based” – based on a sub-advisor’s total assets across all policies.SMA costs do not include investment management or sub-advisor fees nor agent compensation. These fees are also deducted from a PPLI policy’s cash value.

Feature	Insurance Dedicated Funds (IDFs)	Separately Managed Accounts (SMAs)
Investment Control	Managed by Fund Manager	Directly Managed by Advisor
Cost Efficiency	Institutional Pricing	Typically Higher Management Fees
Customization	Moderate	High
Asset Protection	Yes	Yes
Tax Deferral	Yes	Yes

[7] Judas, J. C., & Fontanini, M. PPLI Market Report. Retrieved April 19, 2024, from <https://www.lifeinsurancestrategiesgroup.com/pplimarketreport>.

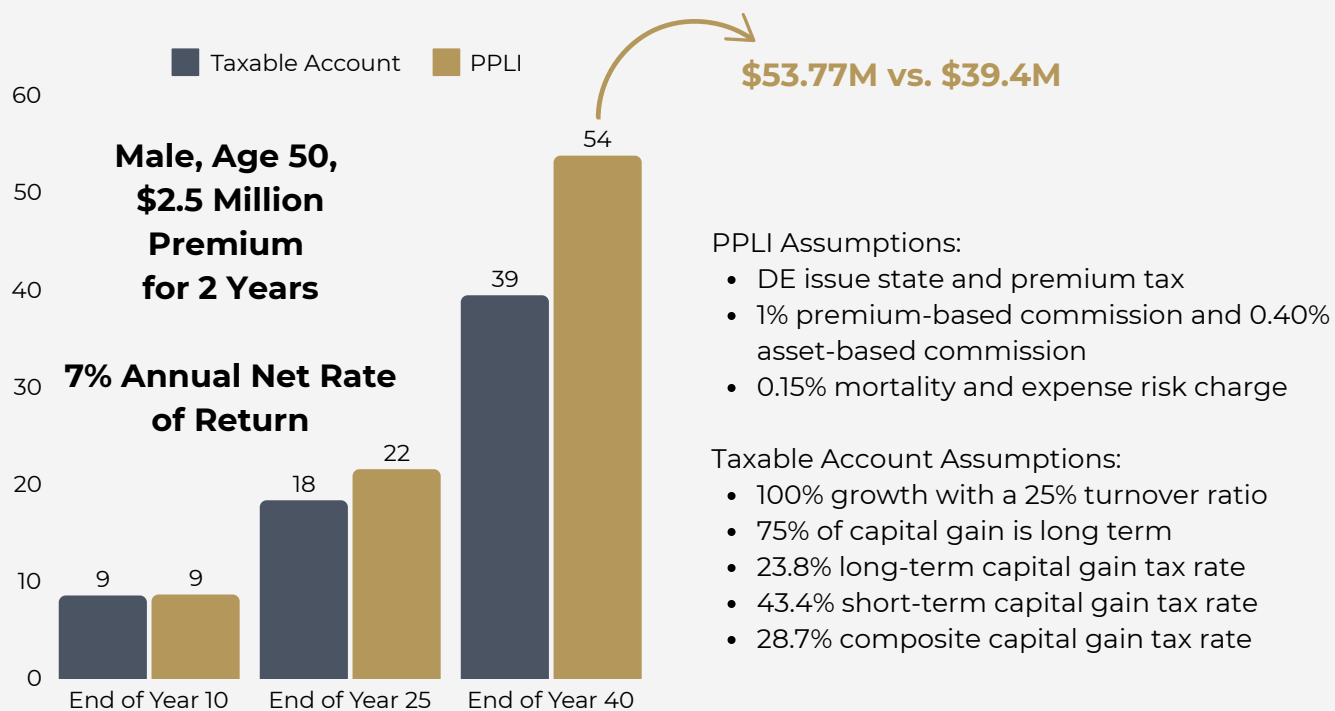
Section 3

Why RIAs and Family Offices Should Use PPLI

Tax Efficiency: Enhancing After-Tax Returns

Tax planning is at the heart of most financial strategies for UHNW individuals, and one of the key appeals of PPLI is its ability to significantly improve after-tax returns. The growth of investments within a PPLI policy is tax-deferred, which means that income and capital gains taxes are not incurred on the assets held inside the policy. This allows the portfolio to compound more efficiently over time.

Additionally, when structured properly, policyholders can access cash values tax-free through policy loans or withdrawals. For clients in high tax brackets, this can translate into substantial savings over the long term. The PPLI structure is particularly appealing for those seeking to hold alternative investments—such as hedge funds or private equity—within a tax-efficient vehicle, as the tax benefits of PPLI extend to these more complex asset classes as well.



Hypothetical example – for illustrative purposes only. Actual results will vary. For financial professional, accredited investor or qualified purchaser use only. Not for use with the public.

Asset Protection: Safeguarding Wealth from Legal and Creditor Risks

Wealthy individuals often have heightened concerns about protecting their assets from lawsuits, creditors, and other legal risks. Depending on the jurisdiction, assets held within a PPLI policy may be protected from creditors and legal claims, offering a vital layer of security. This is especially important for clients in professions that carry a high risk of litigation, such as medical professionals, business owners, and executives.

While asset protection laws vary from state to state and internationally, PPLI can provide robust safeguards when structured appropriately. The ability to shield assets while simultaneously benefiting from tax-deferred growth is one of the reasons why PPLI has become an essential component of comprehensive wealth preservation strategies.

Customization and Control: A Bespoke Solution for the UHNW Market

One of the most attractive features of PPLI is its inherent flexibility. Unlike traditional life insurance policies, which offer limited investment options, PPLI policies allow for almost unlimited customization of the underlying investments. Clients can choose from a wide range of asset classes, including hedge funds, private equity, real estate, and more.

This flexibility enables RIAs and family offices to continue managing their clients' assets according to their specific investment strategies, while taking advantage of the tax-deferred growth afforded by the PPLI policy. Moreover, the policy can be tailored to the client's risk tolerance, time horizon, and liquidity needs, making it a perfect fit for the diverse and often complex portfolios of UHNW individuals.

Estate Planning and Wealth Transfer: Efficiently Passing Wealth to Future Generations

Wealth transfer is a key concern for many ultra-wealthy families, especially when it comes to minimizing the impact of estate taxes. PPLI offers a highly efficient solution for transferring wealth across generations. The death benefit of a PPLI policy is paid out to beneficiaries tax-free, which can provide much-needed liquidity to cover estate taxes or other liabilities upon the policyholder's death.

Additionally, the policy can be integrated into broader estate planning structures, such as trusts, to provide even more control and flexibility over how and when wealth is transferred. This can help clients achieve their legacy goals while ensuring their heirs receive the maximum benefit from their wealth.

Section 4

How RIAs and Family Offices Can Implement PPLI for Clients

Collaborating with Insurance Professionals: Building the Right Team

While PPLI is a powerful tool, it requires specialized knowledge to implement correctly. RIAs and family offices should work in partnership with experienced insurance professionals who understand the nuances of PPLI, including the tax and regulatory complexities.

This collaboration ensures that the PPLI policy is structured in a way that aligns with the client's financial goals while adhering to legal and regulatory requirements. The insurance expert will also assist in determining the appropriate policy size and structure based on the client's needs, whether that includes funding future premiums or managing the timing of premium contributions.

Managing Investments within PPLI: Maintaining Continuity with Customization

One of the major advantages of PPLI is that it allows RIAs and family offices to continue managing their clients' investments. The PPLI policy provides the insurance coverage, but the investment management itself can remain under the RIA's or family office's control. This allows for continuity in investment strategy while gaining the added benefit of tax deferral.

It's important to note that PPLI policies offer flexibility not just in terms of investment choices but also in how those investments are managed. RIAs and family offices can actively manage the assets, rebalance portfolios, and take advantage of alternative investments—such as hedge funds or private equity—that are typically unavailable in traditional life insurance policies. This makes PPLI a unique and adaptable tool for clients seeking tax-efficient growth without sacrificing investment control.

Understanding Costs and Transparency: Debunking the Myths

One of the common misconceptions about PPLI is that it is prohibitively expensive. While it's true that PPLI is designed for UHNW clients, it can be surprisingly cost-effective when compared to other investment vehicles. PPLI contracts are transparent to the owner for pricing of policy charges and investment management expenses. These contracts are often issued directly to purchasers without a sales commission, which can allow the life insurance company to waive the early surrender charges found in retail contracts. Specific to PPLI, the transparency of policy costs permits a potential buyer to evaluate if the higher insurance costs in the early years of the policy are outweighed by the tax savings the policy provides.

Typical costs associated with a PPLI policy include an annual asset-based fee, death benefit charges often referred to as "Cost of Insurance" and, if applicable, federal and/or state tax.

In addition, PPLI policies are structured to be scalable. Clients can contribute premiums based on their individual cash flow and liquidity needs, allowing for flexible funding strategies. For clients with significant income or wealth, the cost of a PPLI policy is often far outweighed by the tax savings and asset protection benefits it provides.

Section 5

Case Study 1: Reducing Tax Exposure for a High-Income Executive

Client Profile:

A successful technology executive, aged 45, earning substantial annual bonuses and stock options. The client's investment portfolio had grown significantly, but he was facing an increasing tax burden on capital gains and dividends. The RIA that handles the executive's investments was looking for a solution that would allow him to continue growing his wealth while reducing his exposure to taxes.

Strategy:

The RIA, working with an insurance specialist, implemented a PPLI policy to shelter a portion of the executive's investment portfolio. By including a mix of equities, alternative investments, and income-producing assets in a SMA inside the PPLI, the executive could defer taxes on the growth of these assets. Additionally, the policy was structured to allow for tax-free withdrawals in the future through policy loans.

Results:

Over a 10-year period, the executive experienced significant tax savings by deferring capital gains taxes and dividend income. The tax savings compounded over time, enhancing the overall growth of the portfolio. In addition, the RIA was able to maintain control over the investment strategy within the PPLI policy, ensuring alignment with the client's broader financial goals. Upon retirement, the executive plans to access the policy's cash value tax-free to finance lifestyle expenses, further enhancing the tax efficiency of the strategy.

Case Study 2: Legacy Planning for a Family Business Owner

Client Profile:

A 65-year-old second-generation family business owner with substantial assets in both liquid and illiquid investments. The client was concerned about estate taxes and wanted to ensure a smooth transition of wealth to her children, while also protecting her assets from potential legal claims.

Strategy:

The family office worked with an estate planning attorney and PPLI specialist to implement a policy that would provide tax-free liquidity at death, sufficient to cover estate taxes. The policy was structured to include both traditional investments and alternative assets, providing the business owner with maximum flexibility in managing her wealth. Additionally, the PPLI policy was housed within an irrevocable life insurance trust (ILIT) to ensure creditor protection.

Results:

The business owner successfully transferred a significant portion of her wealth to her children in a tax-efficient manner. The PPLI policy provided the necessary liquidity to cover estate taxes without having to sell family business assets. Furthermore, the assets held within the PPLI were protected from creditors, ensuring that the business and other personal assets remained intact for future generations. The PPLI strategy not only fulfilled her legacy goals but also provided a secure structure for the continuation of the family business.

PPLI is a Must-Have Tool for RIAs and Family Offices

Private Placement Life Insurance is more than just an insurance product - it's a comprehensive wealth management solution that offers unmatched benefits for tax-efficient growth, asset protection, and estate planning. For RIAs and family offices serving ultra-high-net-worth clients, PPLI provides the flexibility, customization, and control necessary to meet the complex needs of their clientele.

By incorporating PPLI into your practice, you can offer clients a sophisticated financial tool that enhances their investment strategy, protects their wealth, and ensures efficient wealth transfer to future generations. As we have seen in the case studies, RIAs and family offices can incorporate the use of PPLI into their practice to help their clients achieve their goals, all while deepening the relationship between them.

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