Client Conversations – Summer 2023

Q: I bought whole life insurance when my kids were little. Do I still need it?

In brief, maybe you don’t. If your kids have finished college, your mortgage is paid off (or you plan on downsizing), and your retirement savings are on track, you may no longer need your life insurance policy. Still, there are reasons you might want to keep it.

For instance, consider that—simply due to aging—you are now at a higher risk of health complications. Even with health insurance in place, it’s easy to amass tens of thousands of dollars of uncovered healthcare expenses, especially if you need long-term care. Life insurance is one way your spouse and heirs can replenish any depleted savings accounts after these expenses are paid.

You can also use life insurance to pay for estate taxes. Typically, this is done by establishing an irrevocable life insurance trust (ILIT), which is shielded from creditors and the Internal Revenue Service. Or you can leverage life insurance to leave an inheritance for your loved ones by naming them as the beneficiaries of your policy. Another option is to sell the policy through a viatical settlement, but there are some very specific requirements you’ll have to meet before this can happen. Also, a viatical settlement is only recommended if the lump-sum payout you’ll receive is more than the cash value of the policy.

No matter what you decide to do, talk to your financial advisor to be sure your actions are aligned with your financial goals. If your policy is paid up so you’re no longer paying premiums, then you won’t have to do anything to keep it, so you might as well get the full benefit from it. An advisor can help you understand the best way to do that.

Q: Can you explain how FDIC insurance works?

The Federal Deposit Insurance Corporation (FDIC) offers insurance coverage to banks as a way to protect your cash deposits against the risk of bank failure. The standard insurance amount is $250,000 per depositor, per insured bank, for each account ownership category.

In other words, if you have multiple individual accounts at the same bank, the combined total of these accounts is protected up to $250,000. However, if you have more than $250,000 spread across multiple individual accounts at the same bank, only $250,000 would be insured.

Banks aren't required to participate in FDIC insurance, and they aren't insured automatically. They apply for coverage and pay monthly premiums, just like you pay for your health or auto insurance. Banks that choose not to participate in FDIC insurance are extremely rare, but they do exist, so it's a good idea to confirm that your bank is a member.

Credit unions use a separate form of insurance offered via the National Credit Union Administration (NCUA) instead. NCUA coverage is similar to FDIC insurance coverage, guaranteeing up to $250,000 per person, per institution, per ownership category.

To take full advantage of FDIC or NCUA insurance, consider spreading your cash deposits across multiple banks and diversifying your account ownership. These two strategies can help you increase your total insured amount at each bank. And if you're uncertain about how much cash you should have in checking and savings accounts, talk to your financial advisor.

Q: I work at a company that gives me stock as part of my retirement plan. A friend told me about NUA. How does that work?

Net unrealized appreciation (NUA) is a tax strategy that allows you to convert what would usually be considered ordinary income into long-term capital gains instead. Since income tax rates can go as high as 37 percent (plus applicable state income tax), but long-term capital gains tax is capped at 20 percent, this swap can make a big difference to your tax bill.

The strategy allows you to claim long-term capital gains on the difference between the current value of the company stock in your retirement plan and its price when it was originally acquired, also known as its *cost basis*.

One of the other advantages of this strategy is that you do not have to pay both types of tax—income tax and capital gains tax—at the same time. Although income tax will be due when you take your stock out of your company's retirement plan, the long-term capital gains tax on appreciation above the cost basis, known as net unrealized appreciation or NUA, does not happen until the appreciated stock is sold.

Of course, an NUA strategy won't be the right move for everyone. Your plan may not have the necessary features available, or you may not have a low enough cost basis. Also, NUA can only be done after certain triggering events, and you have to follow specific rules to capture the benefits.

As always, the best idea is to consult your financial advisor or tax professional. They can help you understand whether an NUA strategy is suitable for your circumstances and what next steps you'll need to take.