Can Life Insurance Help Provide Retirement Income?

If your children are grown and your mortgage is paid off, do you still need to carry life insurance? It depends on your situation, but for many people, a cash-value life insurance policy, such as whole life or universal life, can be a valuable, tax-efficient source of retirement income.

And by drawing on the cash value of your policy, you might be able to temporarily reduce the amount you take out from your retirement accounts, such as your IRA and 401(k). This ability could be especially important when the financial markets are down — you'd probably like to avoid liquidating your assets when their prices have dropped.

Basically, you can use the cash in your policy in these ways:

• *Withdrawals* – You can typically withdraw part of the cash value of your life insurance without losing coverage. You generally won't incur income taxes on these withdrawals, up to the amount you've put into the policy — that is, the premiums you've paid. Once your withdrawals exceed this amount, you would generally owe taxes. Also, keep in mind that any withdrawals will reduce your policy's death benefit and the available cash surrender value.

• *Policy loans* – Rather than taking a withdrawal from your policy, you could take out a loan. You won't have to go through an approval process or income verification, and policy loans typically have lower interest rates than bank loans and don't assess closing costs. Plus, because your insurer will be lending you the money and using the cash in your policy as collateral, your policy's cash value can remain intact and still potentially grow. However, policy loans do carry some issues of which you should be aware. For one thing, while a loan usually isn't taxable, you could end up owing taxes on any unpaid loan balance, including interest. And if this balance exceeds the policy's cash value, it could cause your policy to lapse. Also, outstanding loans can reduce your death benefit.

• *Cashing out* – If you cash out, or "surrender," your policy, you can receive the entire cash value, plus any accrued interest. You will have to subtract any money needed to pay policy loans, along with unpaid premiums and surrender fees, which can be significant. Also, any amount you receive over the policy's cash basis — the total of premiums you've paid — will be taxed as regular income.

• *1035 Exchange* – Through what's known as a Section 1035 Exchange, you can transfer your life insurance policy to an annuity, which can be structured to pay you a lifetime income stream. The exchange won't be taxable but surrender charges may still apply.

Given the potential tax implications of the above options, you may want to consult with your tax advisor before making any moves. Also, be sure you are comfortable with a reduced or eliminated death benefit. Specifically, you'll want to be confident that your spouse or other family members don't need the proceeds of your policy. This may require some discussions about your loved ones' plans and needs. And don't forget that life insurance can help your family pay for final expenses, such as funeral costs and unpaid medical bills.

Whether it's providing you with needed retirement income or helping your family meet future needs, your cash value life insurance policy is a valuable asset — so try to put it to the best use possible.

This article was written by Edward Jones for use by your local Edward Jones Financial Advisor.

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