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Enhancing understanding of sophisticated planning strategies and their applications.

New Private Placement Opportunities Emerge in 2018

With the momentum of another record year in 2017, private placement life (PPLI) and annuity (PPVA) product activity remains strong in 2018.

Despite headwinds from the Tax Cuts and Jobs Act ("Act") and increased market volatility, other components of the Act make it a good time to consider PPLI and PPVA offerings.

Increased market volatility may drive increased demand for insurance products, which offer alternative assets classes that are non-correlated to traditional markets.

In addition, there are tax considerations that may make PPLI and PPVA even more attractive for clients seeking tax-efficient planning solutions.

For Individuals

- The Act eliminates the ability to deduct miscellaneous itemized deductions, such as investment management fees and expenses. This could have a substantial impact on investors allocating to alternative investments (typically, in a limited partnership structure), which tend to have higher fees and expenses.
- The Act raises effective tax rates for individuals residing in states with high income tax rates by capping the combined deductibility of state and local taxes at $10,000.
- When combined, the higher effective tax rate and elimination of the ability to deduct investment management fees and expenses can result in a substantial increase in taxes. Depending on the state, the effect can be significant.
- For example, a taxable investment solution actually pays more tax as a result of the lost deductions:
  - An individual in the top income bracket living in a higher tax state, e.g. Connecticut, has a 6.99% state tax rate
  - An investment in a taxable fund which earns 6.50% net of investment management fees of 1.50%, i.e. 8.00% gross earnings.
  - Pre-Tax Act the net after tax earnings rate would have been 3.42%
  - Post-Tax Act the net after tax earnings rate will fall to 2.78%

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Impact of Tax Reform on Net Investment Returns		
	PRE-Tax Act	**Post -Tax Act**
Gross Rate of Return	8.00%	8.00%
Management Fee	−1.50%	1.50%
Net Rate of Return	6.50%	6.50%
Federal Tax Rate (39.6%)	−3.17%	−2.96%
Net Inv. Inc. Tax Rate (3.8%)	−0.30%	−0.30%
State Tax Rate (e.g. CT 6.99%)	−0.45%	−0.45%
Deduction for Management Fee	0.65%	0.00%
Deduction for State Income Tax	0.20%	0.00%
Net After-Tax Return	**3.42%**	**2.78%**

For Insurance Companies

- The Act lowers the corporate tax rate from 35% to 21%, which generally helps insurance product pricing.
- The Act also raises taxes on insurance companies by restricting the ability to deduct certain reserves, raising the DAC Tax and changing rules for the calculation of the Dividend Received Deduction. The good news for PPLI and PPVA is that the effect on pricing is negligible when combined with the lower corporate tax rate.

Some planning ideas that make PPLI and PPVA an attractive solution:

- Private Placement offers a broader range of non-correlated asset choices at times of higher market volatility and rising interest rates when compared to registered variable products. Private Placement also offers the same registered investment options available through a registered variable product.
- PPLI remains attractive for clients with investment portfolios of family wealth that will likely be transferred to future generations. This is especially true for investments in asset classes that generate high levels of current taxation.
- A PPVA is ideal for the tax-efficient investing of assets that are earmarked to a private foundation or charity at death without giving up ownership and control during lifetime.
- A PPVA may be a suitable alternative to a retail deferred annuity due to its lower fee structure and broader investment options.

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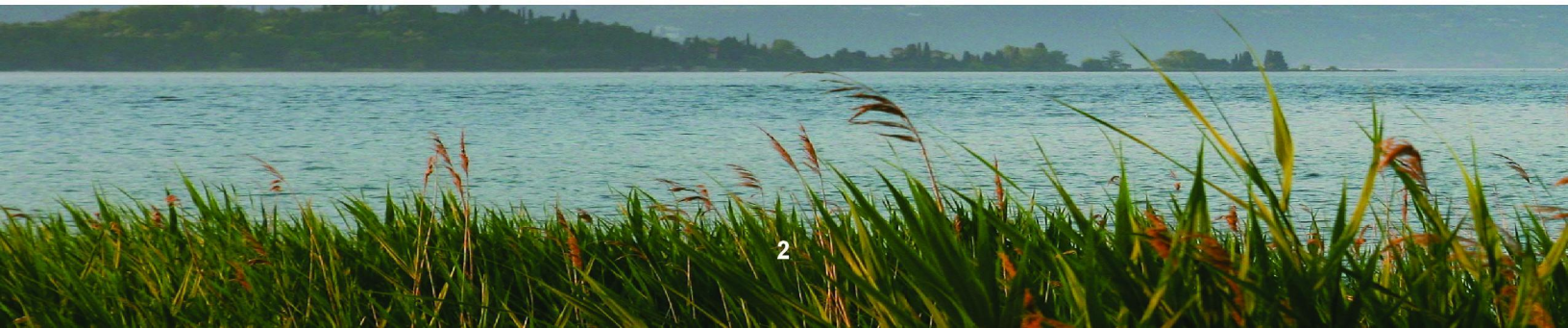

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