

Life Insurance - A Tangled Web

Life Insurance is an interesting product in a few ways, tax free death benefit, the growth inside a policy is not taxed till you take it out, it can be used as asset to fund corporate liabilities and many others. However, Life Insurance is also a complex tool that has a family or a business waiting on those benefits and when it is misunderstood or misused the consequences are usually messy and expensive.

Far too often a Life Insurance product is put in place and then forgotten about; Insureds end up saying something like, "It was something about retirement, but I don't know now and I don't know who to call about it". This case is based on a recent call I received from a CPA. I have changed the names and details to protect the innocent, but it is great example of why Life Insurance is complex and what can happen when it is there is not understood.

JLM, Inc was at the forefront of outsourcing Defense Department IT Services in the mid-80s. John L. Moore was President at the time and Bryan James and James Bryan were his primary revenue generators. In 1990 John made it his goal to sell the company by 2001, he knew he needed to keep James and Bryan to do it. A friend from John's weekend foursome had a brother-in-law who sold insurance for Insurance Carrier Life at the time, and he told John about an idea called a Split Dollar Plan. As it was explained to John, "Basically, JLM would buy a policy each on James and Bryan with a bonus that each of them were deferring into the life insurance policy and if they stayed for 10 years they'd each get all the deferred income plus the growth, which was growing 'tax free'." John bought right into the idea, sat James and Bryan down, explained it to them, and they were underwritten and policies were issued.

Fast forward to 2001, John retires at age 60 after selling JLM to a National Defense Contractor (NDC). James leaves the company at the time of sale. Because there is some complexity to James' exit, the General Counsel at the NDC makes sure to change ownership of James' policy to James when he leaves. James immediately cashes in the policy to pay taxes and some legal bills. Bryan goes on to work for the NDC for 10 more years. In 2011 when NDC is being broken up as part of a failed buyout plan, Bryan retires. Human Resources at NDC offers him the option to continue to pay for his life insurance policy that dates back to the JLM, Inc. days on his own if he wants. However, Bryan's never is assigned ownership of his policy.

In 2015 Bryan becomes very ill and his wife reaches out to Insurance Carrier Life to inquire about Bryan's life insurance policy and possibly using some money from it to pay for medical care. Insurance Carrier Life's customer service team tries to do everything they can, but they can't give Bryan or his wife any information on the policy because they don't own the policy. Insurance Carrier Life is willing to send ownership change forms to JLM; however, JLM no longer exists and NDC is now three different companies. Bryan's wife finally reaches out to an attorney to sort out a conversation with NDC and Insurance Carrier Life.

I've made the point here before that Insurance Contracts are living, breathing legal agreements that continue on well past the day they are sold. This is a perfect example of how that can be missed and families with no insurance, legal or tax training are left to try to figure things out on their own or at great expense.

A number of questions came to mind as I reviewed the case: why didn't the agent stay involved, why didn't JLM's attorney sit down with the agent and John to understand the transaction and write up an agreement to accompany the policies, how did these policies not fall under some scrutiny in the due diligence in the buyout. The failures in the system are numerable, but a simple bit of follow up and service by the agent could have solved many of them. An annual meeting to review the performance of the Split-Dollar policies could have led to a deeper conversation about them at the time of the first sale, and at that time could have led to both policies properly being transferred, saving Bryan and his family time, money, and stress in one of the most difficult times of their lives.

