

The following are the numbers from my newsletter titled: **Life Insurance in Qualified Plans: Calculating the Real Costs will Surprise You.**

Column A is the imputed income an employee has to recapture every year (it's actually slightly less due to the fact that there is imputed income on the first \$50k of death benefit provided by an employer).

Column B is the tax due on the imputed income every year by the employee assuming he/she is in the 40% income tax bracket.

Column C is the pre-tax income the employee needs to take home in order to net enough money to pay income taxes on the imputed income.

Column D is the 30-year level term costs for \$1 million coverage.

Column E is the sum of Column C and D.

Column F is the total amount of money after tax it costs the employee to buy life insurance (in other words, if the employee didn't buy LI in the QP, he/she would have had this much money in his/her pocket after tax).

	A	B	C	D	E	F
	Recapture	Tax Due on	Pre-Tax Take Home	30-Year	Total Pre-Tax Cost	Total After-Tax Out-of-Pocket
	Table 2001 Costs	Imputed Income	Income Needed	Deductible	To Buy Life Ins.	Cost to Buy Life Ins.
Age	(Imputed Income)	40% Tax Bracket	To Pay The Tax	Life Ins. Cost	Inside QP	Inside QP
40	\$1,100	\$440	\$733	\$1,185	\$1,918	\$1,151.0
41	\$1,130	\$452	\$753	\$1,185	\$1,938	\$1,163.0
42	\$1,200	\$480	\$800	\$1,185	\$1,985	\$1,191.0
43	\$1,290	\$516	\$860	\$1,185	\$2,045	\$1,227.0
44	\$1,400	\$560	\$933	\$1,185	\$2,118	\$1,271.0
45	\$1,530	\$612	\$1,020	\$1,185	\$2,205	\$1,323.0
46	\$1,670	\$668	\$1,113	\$1,185	\$2,298	\$1,379.0
47	\$1,830	\$732	\$1,220	\$1,185	\$2,405	\$1,443.0
48	\$1,980	\$792	\$1,320	\$1,185	\$2,505	\$1,503.0
49	\$2,130	\$852	\$1,420	\$1,185	\$2,605	\$1,563.0
50	\$2,300	\$920	\$1,533	\$1,185	\$2,718	\$1,631.0
51	\$2,520	\$1,008	\$1,680	\$1,185	\$2,865	\$1,719.0
52	\$2,810	\$1,124	\$1,873	\$1,185	\$3,058	\$1,835.0
53	\$3,200	\$1,280	\$2,133	\$1,185	\$3,318	\$1,991.0
54	\$3,650	\$1,460	\$2,433	\$1,185	\$3,618	\$2,171.0
55	\$4,150	\$1,660	\$2,767	\$1,185	\$3,952	\$2,371.0
56	\$4,680	\$1,872	\$3,120	\$1,185	\$4,305	\$2,583.0
57	\$5,200	\$2,080	\$3,467	\$1,185	\$4,652	\$2,791.0
58	\$5,660	\$2,264	\$3,773	\$1,185	\$4,958	\$2,975.0
59	\$6,060	\$2,424	\$4,040	\$1,185	\$5,225	\$3,135.0
60	\$6,510	\$2,604	\$4,340	\$1,185	\$5,525	\$3,315.0
61	\$7,110	\$2,844	\$4,740	\$1,185	\$5,925	\$3,555.0
62	\$7,960	\$3,184	\$5,307	\$1,185	\$6,492	\$3,895.0
63	\$9,080	\$3,632	\$6,053	\$1,185	\$7,238	\$4,343.0
64	\$10,410	\$4,164	\$6,940	\$1,185	\$8,125	\$4,875.0
65	\$11,900	\$4,760	\$7,933	\$1,185	\$9,118	\$5,471.0
	\$108,460	\$43,384	\$72,307	\$30,810	\$103,117	\$61,870.0

The following numbers are pretty simple. On the left in the lined boxes are the numbers explaining how much it costs the employee to come out of pocket to buy the same \$1 million DB policy with after-tax dollars.

Column I is the difference in out-of-pocket costs to the employee when buying the LI policy outside of the QP vs. buying it inside the plan (the numbers from inside the plan come from Column F in the previous chart). The difference increases every year because the Table 2001 costs increase every year.

On the right are the side-fund numbers. The side fund is needed because it costs less (except the first few years) for the employee to buy LI outside of the QP. The side fund is needed because it's not enough to add up the cost difference every year. This is a 30-year example; and, therefore, the lost opportunity costs on the difference needs to be calculated. I've assumed the side-fund money grows at 7% annually.

G		H		I		Side Fund Growth				
Pre-Tax Premium Inomce Needed To Pay LI Premium <u>Outside</u> of QP	Total After-Tax Out-of-Pocket Cost to Buy Life Ins. <u>Outside</u> of QP	Annual Difference Between Out-of-Pocket (paying premium in plan vs. out)		age	Start of Year Balance	Contribution	7.00% Growth	Year End Balance		
\$1,975	\$1,185		(\$34)	40	(\$34)	\$0	(\$2)	(\$36)		
\$1,975	\$1,185		(\$22)	41	(\$36)	(\$22)	(\$4)	(\$62)		
\$1,975	\$1,185		\$6	42	(\$62)	\$6	(\$4)	(\$60)		
\$1,975	\$1,185		\$42	43	(\$60)	\$42	(\$1)	(\$20)		
\$1,975	\$1,185		\$86	44	(\$20)	\$86	\$5	\$71		
\$1,975	\$1,185		\$138	45	\$71	\$138	\$15	\$224		
\$1,975	\$1,185		\$194	46	\$224	\$194	\$29	\$447		
\$1,975	\$1,185		\$258	47	\$447	\$258	\$49	\$754		
\$1,975	\$1,185		\$318	48	\$754	\$318	\$75	\$1,147		
\$1,975	\$1,185		\$378	49	\$1,147	\$378	\$107	\$1,632		
\$1,975	\$1,185		\$446	50	\$1,632	\$446	\$145	\$2,223		
\$1,975	\$1,185		\$534	51	\$2,223	\$534	\$193	\$2,950		
\$1,975	\$1,185		\$650	52	\$2,950	\$650	\$252	\$3,852		
\$1,975	\$1,185		\$806	53	\$3,852	\$806	\$326	\$4,985		
\$1,975	\$1,185		\$986	54	\$4,985	\$986	\$418	\$6,388		
\$1,975	\$1,185		\$1,186	55	\$6,388	\$1,186	\$530	\$8,105		
\$1,975	\$1,185		\$1,398	56	\$8,105	\$1,398	\$665	\$10,168		
\$1,975	\$1,185		\$1,606	57	\$10,168	\$1,606	\$824	\$12,598		
\$1,975	\$1,185		\$1,790	58	\$12,598	\$1,790	\$1,007	\$15,395		
\$1,975	\$1,185		\$1,950	59	\$15,395	\$1,950	\$1,214	\$18,559		
\$1,975	\$1,185		\$2,130	60	\$18,559	\$2,130	\$1,448	\$22,138		
\$1,975	\$1,185		\$2,370	61	\$22,138	\$2,370	\$1,716	\$26,223		
\$1,975	\$1,185		\$2,710	62	\$26,223	\$2,710	\$2,025	\$30,958		
\$1,975	\$1,185		\$3,158	63	\$30,958	\$3,158	\$2,388	\$36,505		
\$1,975	\$1,185		\$3,690	64	\$36,505	\$3,690	\$2,814	\$43,008		
\$1,975	\$1,185		\$4,286	65	\$43,008	\$4,286	\$3,311	\$50,605		
\$51,350	\$30,810		\$31,060							

The following is a summary of the numbers and the total increased costs of buying LI inside a QP for an employee in the 40% income-tax bracket. The \$49,939 negative difference includes in the calculation a recapturing of the basis (which equals the taxes paid annually on the economic benefit of the LI coverage).

How much more out of pocket it costs to buy LI in qualified plan?	\$31,060
Lost opportunity cost by not being able to invest the difference every year?	\$50,605
Economic benefit from recapture the Table 1 costs at age 65 assuming a \$108,460 distribution from the QP (assume 40% tax bracket):	\$43,384
Positive or negative financial outcome when buying life insurance in a qualified plan:	(\$7,221)

What if the employee is in the 20% income tax bracket and not the 40%?

As you will see to your surprise, it makes even less sense for a lower tax bracket payer to buy life insurance inside a qualified plan.

	A	B	C	D	E	F
	Recapture	Tax Due on	Pre-Tax Take Home	30-Year	Total Pre-Tax Cost	Total After-Tax Out-of-Pocket
	Table 2001 Costs	Imputed Income	Inomnce Needed	Deductible	To Buy Life Ins.	Cost to Buy Life Ins.
Age	(Imputed Income)	20% Tax Bracket	To Pay The Tax	Life Ins. Cost	Inside QP	Inside QP
40	\$1,100	\$220	\$275	\$1,185	\$1,460	\$1,168.0
41	\$1,130	\$226	\$283	\$1,185	\$1,468	\$1,174.0
42	\$1,200	\$240	\$300	\$1,185	\$1,485	\$1,188.0
43	\$1,290	\$258	\$323	\$1,185	\$1,508	\$1,206.0
44	\$1,400	\$280	\$350	\$1,185	\$1,535	\$1,228.0
45	\$1,530	\$306	\$383	\$1,185	\$1,568	\$1,254.0
46	\$1,670	\$334	\$418	\$1,185	\$1,603	\$1,282.0
47	\$1,830	\$366	\$458	\$1,185	\$1,643	\$1,314.0
48	\$1,980	\$396	\$495	\$1,185	\$1,680	\$1,344.0
49	\$2,130	\$426	\$533	\$1,185	\$1,718	\$1,374.0
50	\$2,300	\$460	\$575	\$1,185	\$1,760	\$1,408.0
51	\$2,520	\$504	\$630	\$1,185	\$1,815	\$1,452.0
52	\$2,810	\$562	\$703	\$1,185	\$1,888	\$1,510.0
53	\$3,200	\$640	\$800	\$1,185	\$1,985	\$1,588.0
54	\$3,650	\$730	\$913	\$1,185	\$2,098	\$1,678.0
55	\$4,150	\$830	\$1,038	\$1,185	\$2,223	\$1,778.0
56	\$4,680	\$936	\$1,170	\$1,185	\$2,355	\$1,884.0
57	\$5,200	\$1,040	\$1,300	\$1,185	\$2,485	\$1,988.0
58	\$5,660	\$1,132	\$1,415	\$1,185	\$2,600	\$2,080.0
59	\$6,060	\$1,212	\$1,515	\$1,185	\$2,700	\$2,160.0
60	\$6,510	\$1,302	\$1,628	\$1,185	\$2,813	\$2,250.0
61	\$7,110	\$1,422	\$1,778	\$1,185	\$2,963	\$2,370.0
62	\$7,960	\$1,592	\$1,990	\$1,185	\$3,175	\$2,540.0
63	\$9,080	\$1,816	\$2,270	\$1,185	\$3,455	\$2,764.0
64	\$10,410	\$2,082	\$2,603	\$1,185	\$3,788	\$3,030.0
65	\$11,900	\$2,380	\$2,975	\$1,185	\$4,160	\$3,328.0
	\$108,460	\$21,692	\$27,115	\$30,810	\$57,925	\$46,340.0

G	H	I	Side Fund Growth				
Pre-Tax Premium Income Needed To Pay LI Premium <u>Outside</u> of QP	Total After-Tax Out-of-Pocket Cost to Buy Life Ins. <u>Outside</u> of QP	Annual Difference Between Out-of-Pocket (paying premium in plan vs. out)	age	Start of Year Balance	Contribution	7.00% Growth	Year End Balance
\$1,481	\$889	\$279	40	\$279	\$0	\$20	\$299
\$1,481	\$889	\$285	41	\$299	\$285	\$41	\$625
\$1,481	\$889	\$299	42	\$625	\$299	\$65	\$989
\$1,481	\$889	\$317	43	\$989	\$317	\$91	\$1,398
\$1,481	\$889	\$339	44	\$1,398	\$339	\$122	\$1,858
\$1,481	\$889	\$365	45	\$1,858	\$365	\$156	\$2,379
\$1,481	\$889	\$393	46	\$2,379	\$393	\$194	\$2,967
\$1,481	\$889	\$425	47	\$2,967	\$425	\$237	\$3,629
\$1,481	\$889	\$455	48	\$3,629	\$455	\$286	\$4,370
\$1,481	\$889	\$485	49	\$4,370	\$485	\$340	\$5,196
\$1,481	\$889	\$519	50	\$5,196	\$519	\$400	\$6,115
\$1,481	\$889	\$563	51	\$6,115	\$563	\$467	\$7,146
\$1,481	\$889	\$621	52	\$7,146	\$621	\$544	\$8,311
\$1,481	\$889	\$699	53	\$8,311	\$699	\$631	\$9,640
\$1,481	\$889	\$789	54	\$9,640	\$789	\$730	\$11,160
\$1,481	\$889	\$889	55	\$11,160	\$889	\$843	\$12,892
\$1,481	\$889	\$995	56	\$12,892	\$995	\$972	\$14,860
\$1,481	\$889	\$1,099	57	\$14,860	\$1,099	\$1,117	\$17,076
\$1,481	\$889	\$1,191	58	\$17,076	\$1,191	\$1,279	\$19,546
\$1,481	\$889	\$1,271	59	\$19,546	\$1,271	\$1,457	\$22,275
\$1,481	\$889	\$1,361	60	\$22,275	\$1,361	\$1,655	\$25,291
\$1,481	\$889	\$1,481	61	\$25,291	\$1,481	\$1,874	\$28,646
\$1,481	\$889	\$1,651	62	\$28,646	\$1,651	\$2,121	\$32,418
\$1,481	\$889	\$1,875	63	\$32,418	\$1,875	\$2,401	\$36,694
\$1,481	\$889	\$2,141	64	\$36,694	\$2,141	\$2,718	\$41,553
\$1,481	\$889	\$2,439	65	\$41,553	\$2,439	\$3,079	\$47,072
\$38,513	\$23,108	\$23,233					

How much more out of pocket it costs to buy LI in qualified plan? \$23,233
Lost opportunity cost by not being able to invest the difference every year? \$47,072
Economic benefit from recapture the Table 1 costs at age 65 assuming a \$108,460 distribution from the QP (assume 20% tax bracket): \$21,692
Positive or negative financial outcome when buying life insurance in a qualified plan: (\$25,380)