TAXATION OF PERSONAL LIFE INSURANCE ACTUAL QUESTIONS AND CORRECT VERIFIED ANSWERS/ALREADY GRADED A+||BRAND NEW!!!

TAXATION OF PERSONAL LIFE INSURANCE- CORRECT VERIFIED ANSWERS-The major tax advantages of life insurance and annuities are:

annual earnings (interest) accumulate on a tax-deferred basis

proceeds payable at death are usually income tax-free to the beneficiary.

If benefits are paid on a qualified accelerated basis due to the insured's terminal illness, they are treated the same as the death benefit would be treated--i.e., they are not taxed. If an annuity owner dies before the annuity has been annuitized, the annuity is passed on to the beneficiary. Only the amount in excess of the policyowner's investment (the interest/gain) is included in the beneficiary's federal income tax liability.

Premiums- CORRECT VERIFIED ANSWERS-As a general rule, premiums paid for either a life insurance or annuity contract are not deductible for federal income tax purposes.

Exception: Qualified IRAs--Premiums paid into a qualified IRA annuity plan are tax-deductible in the year paid in. These funds, along with the tax-deferred interest within the IRA are taxed when withdrawn from the account. If funds are withdrawn before age 59½, there is also a 10% tax penalty that must be paid.

Cash Value Increases- CORRECT VERIFIED ANSWERS-The growth in cash values is tax-deferred under federal income tax law.

Dividends- CORRECT VERIFIED ANSWERS-Dividends are not generally subject to income tax; dividends are taxable only when they exceed the amount of policy premiums that have been paid in (known as the basis). If dividends accumulate at interest, the interest earned is taxable currently.

Policy Loans- CORRECT VERIFIED ANSWERS-Policy loans, except those from Modified Endowment Contracts, are generally not taxable. If a policy is surrendered with a loan outstanding, and if that loan with other cash value is greater than the basis, there is a taxable gain. If a policy lapses, outstanding loans are treated as cash value distributions and are subject to tax on any amount that exceeds the policy's basis.

Surrenders- CORRECT VERIFIED ANSWERS-Withdrawals or partial surrenders from a life insurance policy are usually not taxable as long as the withdrawn amount does not exceed the basis. After the policy's basis has been withdrawn, any other withdrawals are subject to income tax. The contract has FIFO withdrawal status after 10 years (FIFO: first in, first out), meaning that withdrawals are treated as coming first from the basis in the contract.

General Rule and Exceptions- CORRECT VERIFIED ANSWERS-Taxation of death benefit proceeds varies depending on how premiums were paid.

If premiums were paid with after-tax dollars, the proceeds of the insurance policy are income tax-free to the beneficiary upon the insured's death.

If the premiums have been paid with pre-tax dollars, as is sometimes the case with business insurance, the proceeds of the policy are taxable.

Settlement Options- CORRECT VERIFIED ANSWERS-Insurance proceeds paid as a lump sum to the beneficiary upon death are exempt from federal income tax. If another distribution method is chosen and proceeds are paid in installments, each installment will consist of both principal and interest. The interest portion of each payment is taxable as income.

Values Included in Insured's Estate- CORRECT VERIFIED ANSWERS-An insured's estate at the time of death will include:

liquid assets held-savings and other accounts, CDs, stocks and bonds, etc.

fixed assets held-houses, farms, other physical properties, businesses, personal property

other assets-retirement accounts, annuities, life insurance (not included if the owner and beneficiary is someone else) the transfer through gifting of any property including money or the use of or income from property, including assets sold for less than face value and interest-free/reduced interest loans

excluded gifts include-

the first $14,000 (2016) given to one person during a calendar year

gifts for education expenses

gifts for medical expenses

gifts made to spouses, charities, and political organizations.

Taxation- CORRECT VERIFIED ANSWERS-Life insurance policy proceeds are distributed to the beneficiary designated in the policy.

Life insurance proceeds received in a lump sum are received income tax-free.

Life insurance proceeds can also be converted to an annuity and be paid out over time, with interest added to the amount. Each payment has two portions-death benefit and interest. The interest portion of each payment received by the beneficiary in these situations is subject to income tax.

When an annuity is annuitized and payments are made to the annuitant, the IRS has ruled that a fixed portion of each payment (the exclusion ratio) is considered to be return of capital and is not subject to income tax. The portion of each payment considered as interest or growth is subject to income tax.