Private Placement Variable Products – An Introduction

Sophisticated individuals are attracted to high-performing alternative investments for asset diversification. They are also keen on preserving their wealth and capturing as much growth, after tax, on their personal balance sheet. Many of the alternative investments result in short-term capital gains and ordinary income taxes, which effectively reduces the amount received by the investor. The implementation of the Tax Cuts and Jobs Act has additionally impacted the tax-efficiency of these alternatives. As an example, investments that formerly generated a net taxable gain of 8% (after deductions) are now resulting in a taxable gain of 10% due to the elimination of allowable deductions. Individuals are seeking options that enable their assets to grow without incurring such a significant tax drag, especially in states with high state income taxes like New York, California, Illinois, and New Jersey.

Solutions for individuals and their families that desire tax-efficient investing and wealth preservation can be in Private Placement Insurance and Annuity products. These vehicles use "asset location" to defer or eliminate income taxes. When you properly position an individual's assets that generate higher net investment returns, you can immediately unlock significant value, especially for families focusing on future generations. Private Placement Life Insurance (PPLI) and Private Placement Variable Annuity (PPVA) products are key solutions to tax-efficient asset location. "Private placement" means these are unregistered securities and buyers must be Accredited Investors and Qualified Purchasers[1].

The appeal of these products is the ability to access diverse investment alternatives like various hedge fund strategies, private credit funds, private equity, MLPs, real estate equity, ETF strategies, etc. by allocating investments inside the products; these options are in addition to traditional investment funds. Recent developments in the PPVA and PPLI market, including the issuance of IRS guidance on compliant structures have resulted in a significant increase in the number and type of Insurance Dedicated Funds ("IDFs"). Also, the complexity and costs associated with PPVA and PPLI has declined, thereby increasing their accessibility and potential appeal for the investment portfolios of clients.

An Overview

PPLI and PPVA are similar to traditional "retail" variable universal life insurance or a traditional retail deferred variable annuity contract supported by a segregated asset account ("Separate Account"). The PPLI contract makes available various investment fund options (referred to as "Insurance Dedicated Funds" in the case of private investment funds or "Variable Insurance Trusts (VITs) in the case of registered funds). Alternatively, assets can be managed through a "Separately Managed Account" (SMA). An investment manager may manage assets via a customized SMA or IDF established and approved by the insurance company that issues the products. The asset manager has full discretion over the investment management of the SMA in the PPLI or PPVA vehicle. The SMA may invest in a broad range of investments, including equities, fixed income, hedge funds, registered mutual funds, and commodities. The contract owner's Separate Account value varies over time with the investment performance of the investments to which contract premium is allocated. At the end of the day, investment earnings do not incur income tax (and no K-1s) since the accounts are "owned" by the insurance company. There are product fees, which can range from 50 bps (0.50%) to 1% or more but the fees are significantly less than the income taxes that would be incurred on the same investment.

[1] An accredited investor must have had earned income that exceeded $200,000 (or $300,000 together with a spouse) in each of the prior two years and reasonably expects the same for the current year, or, the individual must have a net worth of more than $1 million, either alone or together with a spouse. A qualified purchaser is an individual or family-owned business that owns $5 million or more in investments.

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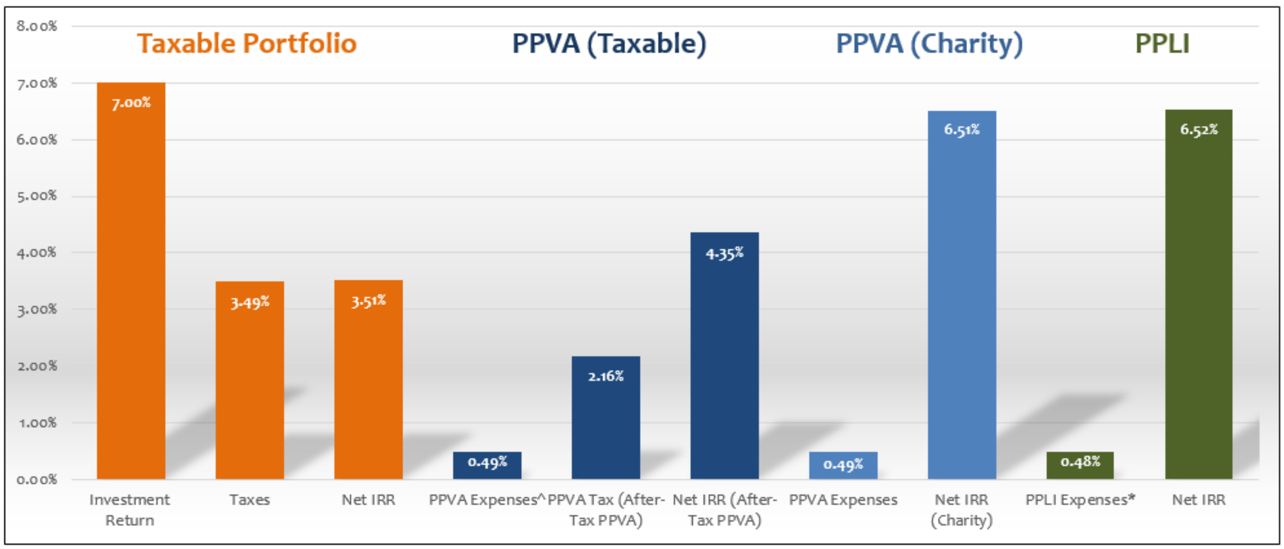
Principal benefits of properly designed and administered life insurance or annuity products is tax deferral as well as creating an ability to transfer wealth without estate taxation (for PPLI). Returns on investments held in PPVAs are not subject to income taxation until death, or when the products are surrendered or withdrawals taken. Additionally, in the case of a properly-designed life insurance contract, death benefit proceeds pass to beneficiaries free of income tax and often free of estate tax also. Additional benefits of PPLI are administrative, in that product owners are generally relieved of tax reporting obligations (e.g., K-1s).

The below table displays how much is retained by the individual when investing in a tax efficient product like PPVA or PPLI versus investing in the similar asset, but held in their taxable portfolio. The table depicts how exceedingly cost-effective PPVA and PPLI are with their ability to mitigate or eliminate the financial drag of taxes. With a properly-structured private placement policy, clients are able to capture returns without the high tax implications typically associated with its taxable alternative. This equals healthy wealth accumulation for a client's lifetime and to preserve wealth for their heirs.

Wealth Preservation from Efficient Asset Location



- All net IRRs calculated over 30 years.
- Assumes 7.00% return on investments. Actual results may vary and are not guaranteed. No current deductions of losses are allowed and ability to deduct losses on surrender or withdrawal may be restricted.
- Assumes ordinary income tax rate of 54.1% comprised of Federal tax rate of 37.0%, Net Investment Income tax rate of 3.8% and CA State income tax rate of 13.3%.
- Assumes capital gains tax rate of 37.1% comprised of Federal tax rate of 20.0%, Net Investment Income tax rate of 3.8% and CA State income tax rate of 13.3%.
- Assumes 75% ordinary income and 25% capital gains per annum.
- The PPVUL policy assumes $10.0 million of premium contributed over 4 years for a non-MEC single life policy issued in SD and a 50-year-old Male insured with preferred underwriting.
- The PPVA policy assumes $10.0 million premium.

Conclusion

Private placement products offer the accredited investor access to both investment alternatives and product designs that may not exist with traditional tax-inefficient investment products. These solutions enable the policyholder to customize the investment options within the contract and provides the policyholder with broader options than typically found in retail variable insurance contracts. The investor can invest in these types of funds without the burden of taxes or the respective tax filing requirements. Private Placement variable products have the potential to convert highly-inefficient taxable assets into favorable tax-efficient investments.

Private Placement Life Insurance (PPLI) Account is an unregistered securities products and is not subject to the same regulatory requirements as registered products. As such, a PPLI Account should only be presented to accredited investors or qualified purchasers as described by the Securities Act of 1933.

This material is intended for informational purposes only, should not be construed as legal or tax advice, and is not intended to replace the advice of a qualified attorney or tax advisor. The information in this presentation is for educational purposes only and is not intended as a solicitation.

A PPLI Account combines the protection and tax advantages of life insurance with the investment potential of a comprehensive selection of variable investment options. The insurance component provides death benefit coverage and the variable investment component provides you the flexibility to potentially increase the PPLI Account's surrender and loan value.

The IRR on the Account Value, Liquidity Value, or Insurance Benefit is equivalent to an interest rate (after taxes) at which an amount equal to the illustrated premium payments could have been invested outside the policy to arrive at the Account Value, Liquidity Value, or Insurance Benefit of the policy.

These calculations make assumptions as to future investment returns, mortality costs, and administrative expenses and are not guaranteed. Actual results may be higher or lower than illustrated. Loans and partial withdrawals will decrease the death benefit and cash value and may be subject to PPLI Account limitations and income tax.

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The tax rates and tax treatment of earnings may impact comparative results. Lower maximum tax rates on capital gains and dividends would make the investment return for the Taxable Account more favorable, thereby reducing the difference in performance between the accounts shown. Investments in securities involve risks, including the possible loss of principal. When redeemed, units may be worth more or less than their original value.

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The financial illustrations and other statements within this report, as well as comments made by any individuals, are not guaranteed and do not constitute a contract. Any contract entered into is between the PPLI Account owner and the insurance company, through its PPLI policy.

You should read the PPLI Account contract and offering documents thoroughly.

Investors should consider the investment objectives and horizons, income tax brackets, risks, charges, and expenses of any variable product carefully before investing. This and other important information about the investment company is contained in each fund's offering memorandum, which can be obtained by calling 602.468.9667. Please read it carefully before you invest.

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File# 2702695.1