Foresters Advantage Plus Whole Life Insurance Dividends

Questions & Answers

Certificate premiums are calculated to provide some margin over the anticipated cost of insurance protection. This is affected by factors such as mortality experience, control of expenses and return on investments. Dividends, in effect, represent a return of a portion of the Owner's premium payments when the above factors are better than anticipated.

Dividends are payable on the certificate anniversary, however there is often no dividend credited on the certificate's first, and sometimes even second, anniversary. For Foresters Advantage Plus Whole Life Insurance, dividends are payable on certificates beginning on the second anniversary for Paid-up at 100 and on the first anniversary for 20-Pay.

Although dividends are expected, they are not guaranteed. In addition, the dividend scale is not guaranteed and will change a number of times during the lifetime of an inforce participating certificate. Foresters™ performs annual dividend reviews and adjusts the scale when deemed necessary.

The Owner determines how dividends are to be applied by selecting a dividend option on the application. At any time, the Owner may change the dividend option by making a written request to Foresters. The new election becomes effective on the next certificate anniversary. The Owner can choose one of the following options:

- Paid-up Additions
- On deposit with interest
- Reduce premium payments
- Paid as cash.

There are no immediate tax implications if dividends are used for Paid-up Additions, to reduce premium payments, or paid in cash. There may be tax implications on these dividend options if the certificate is surrendered, the face amount is decreased, if there is withdrawal of Paid-up Additions, or the certificate lapses.[1]

In the following example, the dividends taken as cash are subtracted from the premiums paid:

Example:
FULL SURRENDER (dividend option paid as cash)
Death Benefit = $40,000
Cash Value = 5,000
Premium Paid = 3,000
Dividends taken as cash on life cert. = 500
Reportable Gain = 5000 – (3000 – 500) = 2,500

In this next example, the death benefit and cash values include the Paid-up Additions purchased by dividends.

Example:
FULL SURRENDER (dividend option is Paid-up Additions)
Death Benefit = $40,000
Paid-up Additions = 3,000
Cash Value = 5,500
Premium Paid = 3,000
Dividends taken as cash = - 0 -
Reportable Gain = 5500 – 3000 = 2,500

Upon surrender, any dividends used to purchase Paid-up Additions will be accounted for since they increase the cash value of the certificate.

Purchase Paid-up Additions

This dividend option is frequently the most desired dividend option for a whole life certificate.

Under this option, the annual dividend is applied as a single premium to purchase paid-up insurance at the Insured's attained age. Values for the Paid-up Additions on Foresters Advantage Plus are based on the 2001 CSO mortality tables at 4% interest in all years. They vary by male, female, and insurance class. Juvenile issue ages are split by male and female, but do not have different insurance classes. Montana has unisex rates.

Paid-up Additions can be surrendered with the cash value payable to the Owner, which may be subject to taxation.

[1] This information is not provided to be used and it cannot be used for the purpose of avoiding penalties that may be imposed on a taxpayer. Foresters, their employees and life insurance representatives, do not provide, on Foresters behalf, legal or tax advice. The information given here is merely a summary of our understanding of current laws and regulations. Advise your clients and prospective purchasers to consult their tax or legal advisor.

Dividends on Deposit

An Owner may leave "dividends on deposit" with Foresters to accumulate with interest. Foresters determines the effective annual rate, but there is a guaranteed minimum interest rate. However, any interest that the Owner earns under this dividend option is taxable; a 1099INT will be issued each year for the earned interest. If the Insured dies, the face amount of the certificate is paid, plus the amount of accumulated dividends (less any outstanding debt). In the event of surrender the certificate's cash value plus the accumulated dividends will be paid to the Owner (less any outstanding debt).

Reduce Premium

When an Owner elects to apply their dividend to "reduce premium", the premium will be reduced by the amount of the annual dividend. Any excess dividend will be applied to any of the other dividend options as chosen by the Owner. If the dividend is less than the premium, the Owner will be billed for the difference.

Paid in Cash

When an Owner elects to receive "dividends in cash", Foresters mails a check for the amount of the annual dividend to the Owner each year. A 1099INT will not be issued to the member, as this dividend option is not considered a reportable event.

FAQ

Are dividends on certificates taxable as income?

No, up to the certificate Owner's cost basis for dividends paid in cash or remaining on deposit. Dividends used to purchase Paid-up Additions are not considered a taxable distribution. If those Paid-up Additions are subsequently surrendered, it is considered a distribution and there may be a reportable tax gain.

Generally, all dividends paid or credited before the maturity or surrender of a contract are tax-exempt as return of premium until an amount equal to the certificate Owner's basis has been recovered.

In other words, when aggregate dividends plus all other amounts that have been received tax-free under the contract exceed aggregated gross premiums, the excess is taxable income. IRC Sec 72(e)(5); Treasure. Sec. 172-11(b)(1).

Is interest on accumulated dividends on deposit taxable?

Yes, interest on accumulated dividends must be included in your client's gross income for the first year which the interest income can be withdrawn, whether or not your client withdraws it. Foresters will send out a 1099INT each year to report interest earned. Treas Reg. Sect. 451-2.

What are the tax results when life insurance or endowment dividends are used to purchase Paid-up Additions?

Normally, no tax liability will arise at any time. Dividends not in excess of investment in the contract are not taxable income (however, different rules apply if the contract is a MEC). The annual increase in the cash value of the Paid-up Additions is not taxable to the certificate holder and death proceeds are tax-free. IRC Sec 72(e). In effect, dividends reduce the cost basis of the original amount of insurance (and constitute the cost of the Paid-up Additions). Upon maturity, sale or surrender during the Insured's lifetime, gross premiums are used as the cost of insurance in computing gain upon the entire amount of proceeds, including proceeds from the Paid-up Addition.

They are treated in the same manner as other insurance. Proceeds are includable in the Insured's estate if they are payable to or for the benefit of his or her estate or if the Insured has any incidents of ownership in the certificate at the time of death.

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