

Combine the advantages of life insurance with the benefits of dismemberment

Aurélie BIECHE • Wealth planner
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Life insurance is a product which is very much appreciated by the French, both for its advantages as a capital accumulation vehicle for holding savings, but also for its advantages in terms of wealth transfer and of wealth planning.

In terms of wealth transfer, the legal technique of dismemberment of ownership (or simply 'dismemberment') is also often favoured by the French, in particular for the advantages it provides on an economic, civil and fiscal level.

Life insurance and dismemberment may be combined and used together to take advantage each other's benefits and characteristics in order to achieve optimal wealth transfer. However, it is vital to ensure that the rights of each party are properly respected.



What is dismemberment?

Dismemberment consists in dividing the ownership of a property into usufruct (the right to use and enjoy a property) and bare ownership (the right to dispose of a property and to become full owner at the end of the usufruct).

Dismemberment is defined by law in Articles 578 et seq. of the Civil Code which provide that it may be established by law or by the intention of the parties and may apply any type of property, including life insurance policies.

How to use dismemberment with a life insurance policy?

In connection with a life insurance policy, ownership may be divided at two levels:

- At the policy subscription level, when the policy is entered into, we refer to a life insurance policy subscribed in dismemberment between the usufructuary and the bare owner;
- At the end of the policy, in the beneficiary clause, when refer to the drafting of a dismembered beneficiary clause.

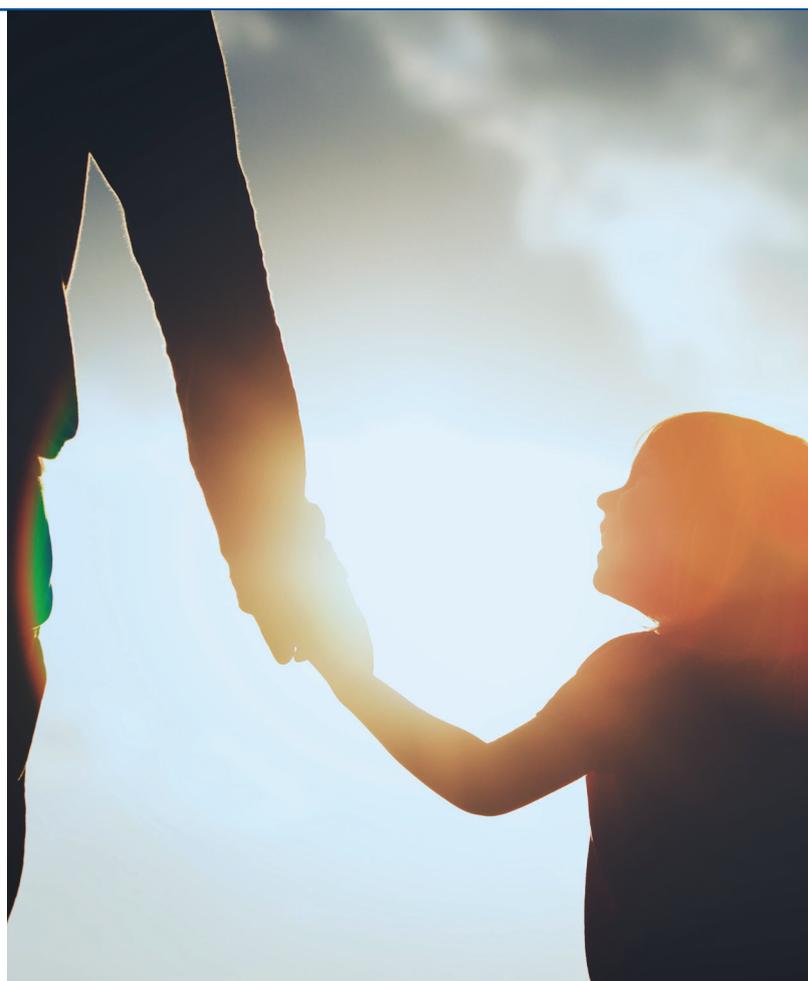
Subscription

The subscription of a life insurance policy in dismemberment may be accepted by insurance companies provided the capital used to subscribe to the policy is already held in dismemberment prior to subscription. For example:

- when capital is re-invested following an inheritance in which the spouse has opted for usufruct,
- the re-investment of capital from the sale of real estate held in dismemberment,
- following a donation.

The subscription will then be made jointly by the usufructuary and the bare owner, each becoming a co-subscriber to the policy.

In practice, it is necessary that a dismemberment agreement be signed between the usufructuary and the bare owner, in addition to the policy. This agreement makes it possible to define the rights of each individual and to ensure that these are properly respected. This agreement is intended in particular to define the income to which the usufructuary is entitled. Indeed, one of the main rights of the usufructuary consists in being able to receive and use the income from the property which is



subject to the dismemberment. Since a life insurance policy does not distribute income as such, this will then be defined by in the dismemberment agreement. Generally, and in order to respect the rights of the bare owner who must, in time, become the owner of the capital, it is provided that the income will be equal to the capital gain in the policy between its current value and the value of the premiums paid. The usufructuary may therefore be free to make surrenders of the policy up to the amount of the capital gain, but must obtain the agreement of the bare owner to surrender larger amounts. The dismemberment agreement may also make it possible to define the rights of each party regarding the ability to make switches, to make changes to the policy's investment policy or even the use the policy as collateral...

Subscription under dismemberment also requires that the person designated as the insured (in principle the bare owner) be vigilant. Finally, particular attention must be paid to the drafting of the beneficiary clause, in order to ensure that each person's rights are respected and that ownership is dismembered if the bare owner dies beforehand

The beneficiary clause

Dismembered beneficiary clauses are, in principle, drafted in a different context. Indeed, in such cases the life insurance policy is subscribed with capital fully owned by the subscriber. The latter chooses to draft a dismembered beneficiary clause with the aim of optimising the transfer of capital from his life insurance policy. This type of drafting of beneficiary clauses is frequently encountered in cases where one of the spouses takes out a life insurance policy and wishes that, when they die, their spouses are able to benefit from the capital under the policy in order to meet their needs and maintain their lifestyle, while optimising the transfer of inherited assets in favour of their children.

In such situations, surviving spouses will then be nominated as the beneficiary of the policy for the usufruct of the capital and the children will be nominated as the beneficiaries for bare ownership of the capital. On the death of the subscriber, the lump sums will be paid in accordance with this clause. As a result, different options for the allocation of the capital may be considered. Indeed, it will be possible:

- either to allocate the capital to each of them, up to the amount of their respective rights in accordance with the value of the usufruct and of the bare ownership on the day of death;
- or to maintain the dismemberment by reinvesting the capital in a new asset, such as a securities account, an accumulation policy or even a property;
- or to grant a quasi-usufruct to the surviving spouse.

It is important that the policyholder's intention regarding either the option to be chosen or the person who will choose the option (usually the usufructuary) be clearly defined in the beneficiary clause in order to enable the insurance company to pay the lump sum on death without any uncertainty.

The drafting of beneficiary clauses is a very personal choice for policyholders who must decide how best to accommodate their intentions and situation. Although widely used and appreciated, the choice of the drafting of a dismembered beneficiary clause may not reflect each family's situation and must be adapted and drafted precisely in order to achieve the desired objectives.

The use of dismemberment for a life insurance policy makes it possible to solve many inheritance problems and is one of the most frequently encountered asset transfer schemes. However, an analysis must be made of each person's situation in order to benefit from all the advantages of this solution.

Do you have a question? Do you want a tailor-made solution? Do not hesitate to contact Baloise Vie Luxembourg.

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www.baloise-international.lu

| Baloise Vie Luxembourg S.A. | 23, rue du Puits Romain | L-8070 Bertrange |
| Tél. +352 290 190-1 | Fax: +352 290 190 462 | www.baloise-international.lu |

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