

# Wealth Transfer Planning: *Creating Flexibility in Uncertain Times*

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## Current planning environment

### Current Exclusions/Exemptions

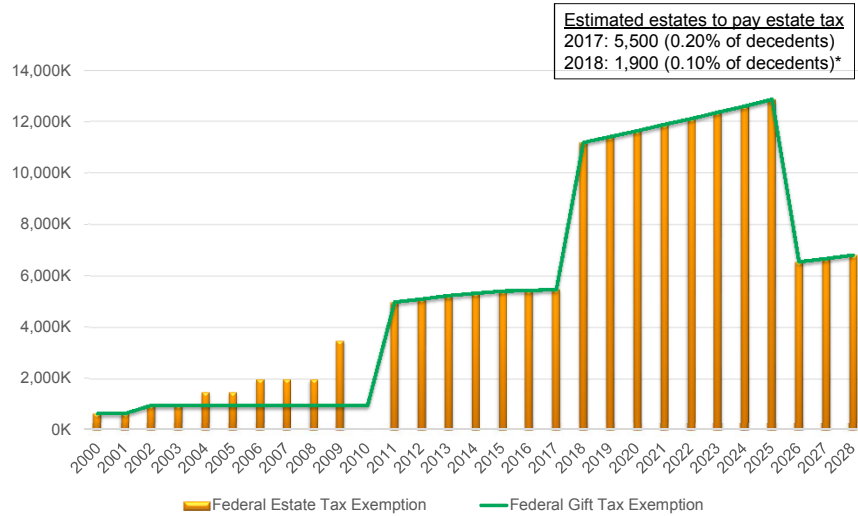
- Annual Exclusion amounts
  - \$15,000/individual
  - \$157,000 for non-citizen spouse
- “Basic Exclusion Amount” (BEA) = \$11,580,000
  - Post tax reform – BEA is \$10M indexed for inflation
  - Scheduled to revert to \$5M indexed for inflation on 1/1/2026
  - For NRAs- limited to \$60,000 exemption (unless provided otherwise in treaty)
- Generation Skipping Transfer Tax (GSTT) exemption = \$11,580,000
  - Scheduled to revert with BEA on 1/1/2026
  - No portability
- Deceased Spouse Unused Exclusion Amount (DSUEA)
  - Additional exemption available if elected on timely filed Form 706



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## Limited window of opportunity ...maybe



Gleckman, Howard (2017, December 6). Only 1,700 Estates Would Owe Estate Tax in 2018 Under the TCJA. <https://www.taxpolicycenter.org/taxvox/only-1700-estates-would-owe-estate-tax-2018-under-tcja>

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## Outright gifting opportunities with life insurance

- Gift cash to trust to pay premiums
- Gift assets to trust and use income to pay premiums
- Gift existing insurance policies to remove from the estate (or from business when no longer needed)
- Seed gifts for sale to defective trust – use income from assets to fund life insurance need
- Forgive a split dollar receivable or previous sale receivable
- Exit a premium financing deal
- Allocation of GST exemption for previously unreported gifts

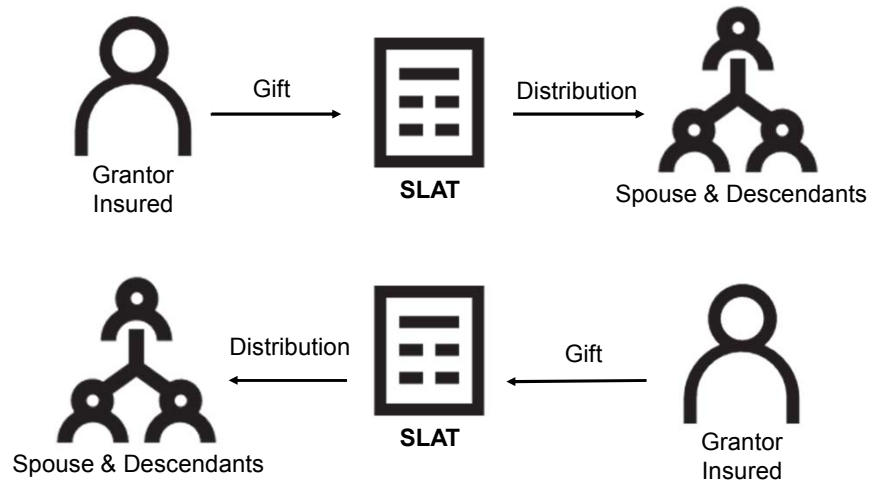
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# Spousal Lifetime Access Trusts

## Spousal access provisions\*



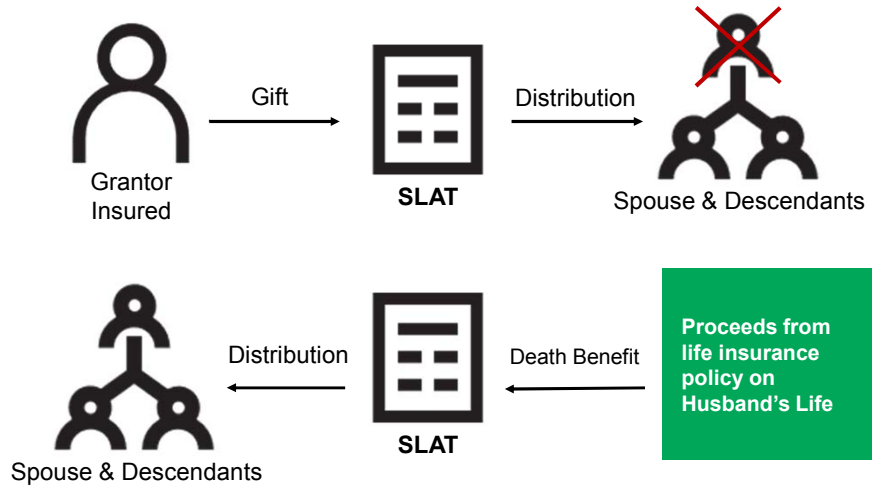
\* Care should be taken to avoid the reciprocal trust doctrine when each spouse creates a trust for the other's benefit

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# SLATs

## Spousal access provisions – Death of first spouse

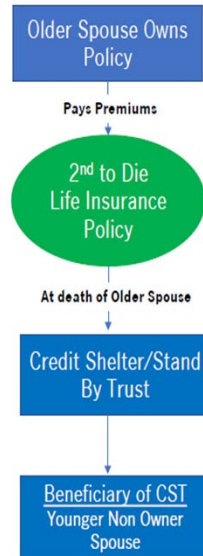


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# Standby Trusts

## Stand By Trust – Mechanics and Benefits



- During Older Spouse Lifetime**
- Older spouse pays premiums from personal funds – no gifts
  - Retains right to Policy Cash Value
  - Retains right to change beneficiary at any time and for any reason (e.g., upon an out of order death)
  - Option to transfer policy at anytime at FMV to CST as “Wait and See Planning” or if out of order death occurs
  - Trust is named as contingent owner and beneficiary

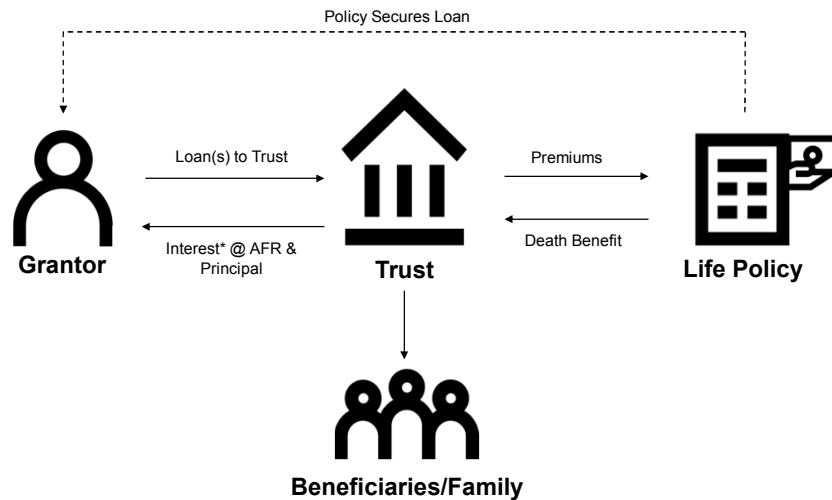
- Upon Death of Older Spouse (assumes 1<sup>st</sup> to die)**
- FMV included in Older spouse’s estate
  - Policy Ownership transferred automatically to CST at FMV and outside of younger spouse’s estate
  - Trustee controls policy for benefit of CST beneficiaries (younger spouse/children/grandchildren)
  - Depending on policy design, trustee may access policy cash value and make distributions to trust beneficiaries per trust terms
  - At second death, death benefit paid to CST free of estate and income taxes



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# Private Financing



\*No recognition of income on interest payments when Trust is a “grantor defective” trust

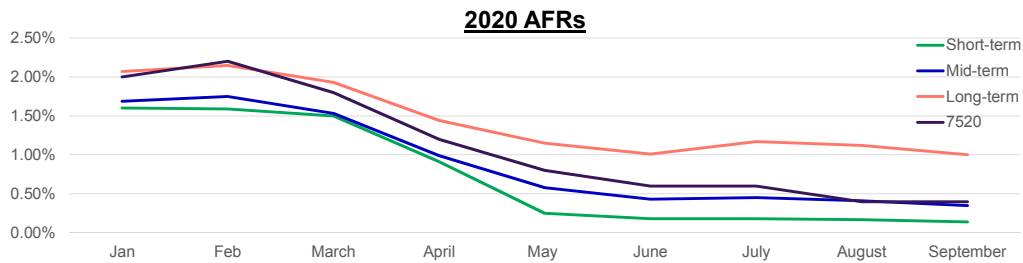
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## Planning in a low interest rate environment

| 2020 AFR RATES          | Sept  | Aug   | July  | June  | May   | April | March | Feb   | Jan   | 20 YEAR AVERAGE* |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|------------------|
| Short term (0-3 years)  | 0.14% | 0.17% | 0.18% | 0.18% | 0.25% | 0.91% | 1.50% | 1.59% | 1.60% | 1.89%            |
| Mid term (4-9 years)    | 0.35% | 0.41% | 0.45% | 0.43% | 0.58% | 0.99% | 1.53% | 1.75% | 1.69% | 2.81%            |
| Long term (10 years +)  | 1.00% | 1.12% | 1.17% | 1.01% | 1.15% | 1.44% | 1.93% | 2.15% | 2.07% | 3.79%            |
| 7520 rate (GRATs/CLATs) | 0.40% | 0.40% | 0.60% | 0.60% | 0.80% | 1.20% | 1.80% | 2.20% | 2.00% | 3.39%            |



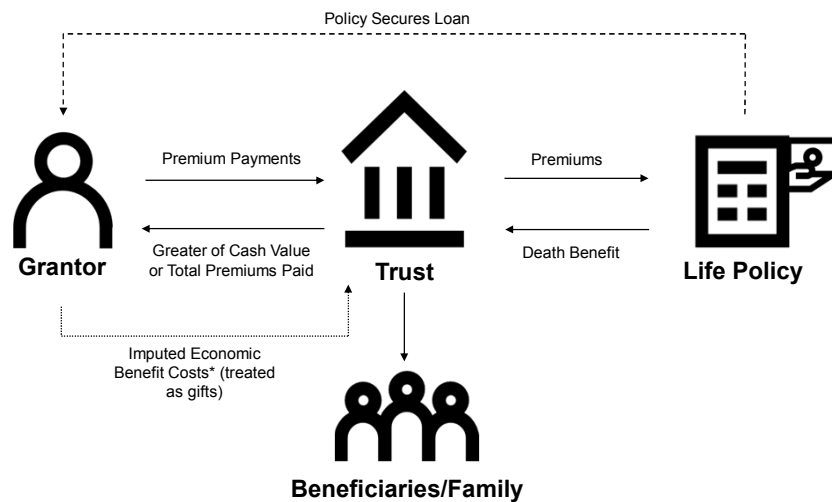
\* Source IRS.Gov – Average determined based on rates from August 2000 – August 2020



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## Private Split Dollar



\*\*Determined based on net amount of DB payable to the trust each year, economic benefit rates (Table 2001 or carrier alternative term rates), and insured's age  
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## Economic Benefit Rates on Survivorship\*

Per \$1,000 of Insurance using Table 2001-10 Rates converted for two lives:

| Insured #1 Age | Insured #2 Age | EB Factor Per \$1,000/insurance | Cost Per \$1M of DB |
|----------------|----------------|---------------------------------|---------------------|
| 40             | 35             | .001116                         | \$1.15              |
| 45             | 40             | .001402                         | \$1.40              |
| 50             | 45             | .003607                         | \$3.61              |
| 55             | 50             | .009784                         | \$9.78              |
| 60             | 55             | .027692                         | \$27.69             |
| 65             | 60             | .079406                         | \$79.41             |
| 70             | 65             | .251512                         | \$251.51            |
| 75             | 70             | .698528                         | \$698.53            |
| 80             | 75             | 1.848288                        | \$1,848.29          |

Survivorship Economic Benefit Rates are calculated by applying the Greenberg to Greenberg calculation to the government Table 2001 rates. Upon the death of one insured, rates would be determined using the single life rates articulated in Table 2001 or using the carrier's alternative term rates (if available and are determined to meet all the requirements for use as articulated in Notice 2002-8.



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# Case Study- The "4-Play"



## Client Profile

**Mr. & Mrs. Smith** (Age 58, PNS; Age 55, PNS) have a \$73M estate consisting mostly of:

| ASSET TYPE               | FMV                               |
|--------------------------|-----------------------------------|
| Commercial RE (100%)     | \$25M (7.5% cash flow; 2% growth) |
| Other Business interests | \$15M (6% cash flow; 2% growth)   |
| Liquid assets/Securities | \$20M (2% cash; 4% growth)        |
| Qualified Plan Assets    | \$3M (4% growth)                  |
| Other personal assets    | \$10M                             |



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### Additional Information

- 3 children – Ages 18, 22, 25
- Limited prior gifting – **almost all exemptions** available
- Currently only own term insurance
- Concerned about liquidity issues upon their death
- Advisor proposing \$30M of second to die insurance coverage owned outside the estate
- Illustrating a survivorship indexed universal life product – 9 pay premium of approximately \$384,895 (illustrated at 5.92%)
  - Purchases \$30M of death benefit
  - IRR @ LE (Ages 95/92) = 6.71% (10.33% pre-tax equivalent)\*

***Despite large exemption, client's looking for efficiency in transferring assets outside of the estate to pay for insurance***

***Let's look at 4 options***

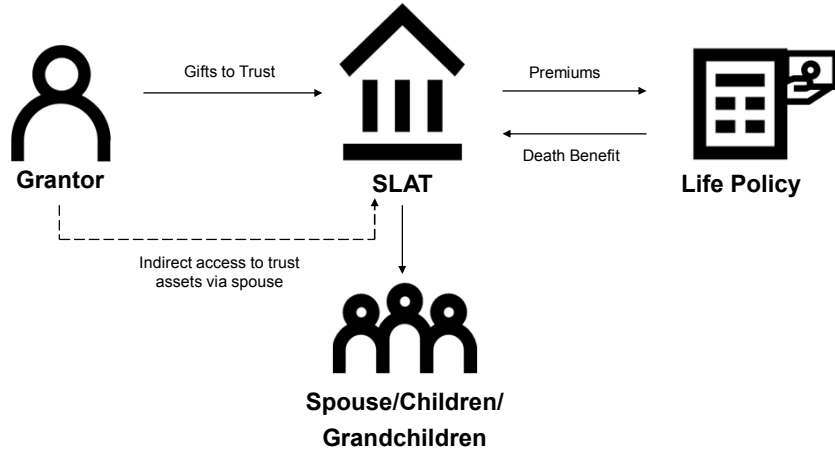
\*The IRR on death benefit is equivalent to an interest rate at which an amount equal to the illustrated premiums could have been invested outside the policy to arrive at the net death benefit of the policy.



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# Gifting to Spousal Access Trust



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## By the Numbers

| YEAR          | GIFT              | APPROXIMATE PREMIUM | DEATH BENEFIT     | CASH VALUE | TRUST SIDE FUND @6% (EOY) | NET TO HEIRS FROM ESTATE | TOTAL NET TO HEIRS | BENEFIT OVER "CURRENT STRATEGY" |
|---------------|-------------------|---------------------|-------------------|------------|---------------------------|--------------------------|--------------------|---------------------------------|
| 1             | 11,580,000        | (384,895)           | 30,000,000        | 0          | 11,866,811                | 42,958,080               | 84,824,891         | 30,008,891                      |
| 5             |                   | (384,895)           | 30,000,000        | 876,083    | 13,196,782                | 49,468,093               | 92,664,875         | 30,111,478                      |
| 10            |                   |                     | 30,000,000        | 2,484,181  | 15,768,390                | 54,549,962               | 100,318,352        | 30,851,652                      |
| 15            |                   |                     | 30,000,000        | 3,620,268  | 21,101,662                | 66,368,370               | 117,470,032        | 33,956,706                      |
| 20            |                   |                     | 30,000,000        | 5,227,354  | 28,238,784                | 80,747,270               | 138,896,054        | 38,292,860                      |
| 25            |                   |                     | 30,000,000        | 7,369,862  | 37,789,863                | 98,241,401               | 166,031,264        | 44,635,633                      |
| 30            |                   |                     | 30,000,000        | 9,967,879  | 50,571,362                | 119,525,685              | 200,097,047        | 53,456,114                      |
| 35            |                   |                     | 30,000,000        | 12,478,963 | 67,675,890                | 145,421,271              | 243,097,161        | 65,187,813                      |
| 37 (LE)       |                   |                     | 30,000,000        | 13,412,393 | 76,040,630                | 157,287,647              | 263,328,277        | 71,090,512                      |
| <b>Totals</b> | <b>11,580,000</b> | <b>(3,464,055)</b>  | <b>30,000,000</b> |            |                           |                          |                    |                                 |



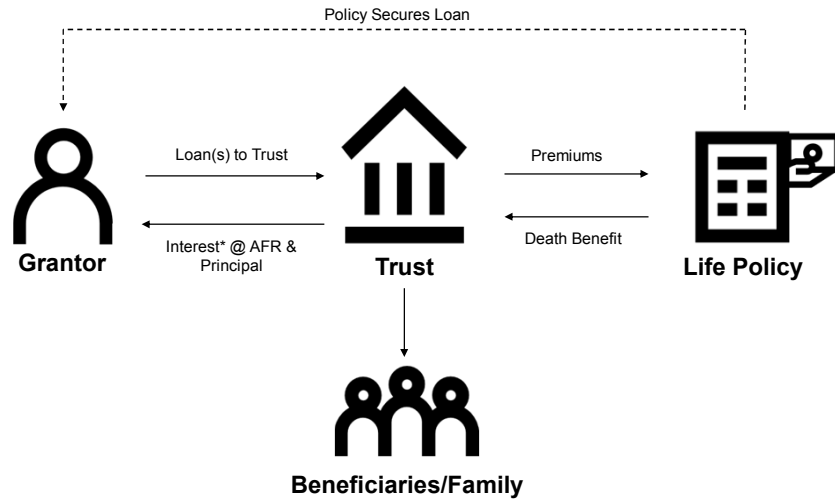
The figures used in this case study are hypothetical, for discussion purposes only, are not guaranteed and may not be used to project or predict results. Actual results may be more or less favorable. Specific product and policy elements would be found in a policy illustration provided by an insurer. With any decision regarding the purchase of life insurance, a client would need to determine which type of life insurance product is most suitable for their specific needs.

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## Private Financing



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## Structuring the Loan & Trust

- Mr. Smith (Grantor) creates ILIT for the benefit of wife and children; independent trustee appointed
- Grantor lends cash to trust using **9 Year AFR term loan**
- Amount transferred = **\$7,527,478**
- May 2020 mid term **AFR 0.58%**
- Asset generates **annual income at 6%**
- Asset income pays:
  - **Loan interest (\$43,659)**
  - **Pays approximate premium (\$384,895)**
- Interest payments back to Grantor help provide resources towards on-going income tax liability

### Benefits

- Leverages lower interest rates compared to bank financing
- Clients in control of the deal
- Places policy in force today
- Provides grantor with flexibility to decide:
  - When to make the gift via forgiveness of loan
  - **NOT** to make the gift and get repaid via loan terms

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## By the Numbers

| YEAR | LOAN        | INTEREST PAID (EOY) 0.58% | GIFT | APPROXIMATE PREMIUM (BOY) | WITHDRAWAL TO PAY PREMIUM & INTEREST | TRUST SIDE FUND ASSET VALUE @ 6%* (EOY) | DEATH BENEFIT | NET TO HEIRS |
|------|-------------|---------------------------|------|---------------------------|--------------------------------------|---|---------------|--------------|
| 1    | 7,527,467   | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 2    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 3    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 4    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 5    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 6    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 7    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 8    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 9    |             | 43,659                    | 0    | 384,895                   | 428,554                              | 7,527,467                               | 30,000,000    | 30,000,000   |
| 10   | (7,527,467) | -                         | 0    | (3,464,055)               |                                      | -                                       | 30,000,000    | 30,000,000   |

Flexibility to use exemption along the way, if desired

\*Trust income includes 2% cash flow and 4% growth on assets.

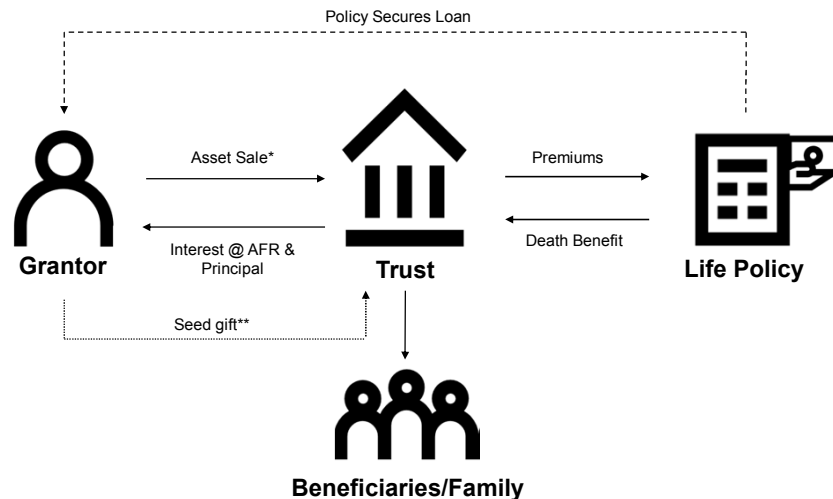
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## Sale to a Grantor Trust



\*No recognition of gain on sale or interest payments when Trust is a "grantor defective" trust

\*\* Usually equal to at least 10% of the FMV of assets to be sold

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## Structuring the Sale

- Mr. Smith (Grantor) creates ILIT for the benefit of wife and children; independent trustee appointed
- Funds trust with “seed gift” - 10% of discounted sale value **[\$560,000]**
- Grantor **sells 32% of commercial RE** business to trust in return for promissory note at long-term **AFR (1.15% for May 2020)**
- Amount transferred = \$8,000,000 (**discounted value \$5.6M**)
- Asset generates **annual income at 7.5%** -use income to life premiums
- Interest payments back to Grantor help provide resources towards on-going income tax liability

### Benefits

- Provides option for long-term estate freeze on assets sold – reducing future estate tax exposure
- Discounting of assets (when available) allows more assets to be transferred for reduced cost
- Provides grantor with flexibility to decide to forgive all/portion of the promissory note to make use of expiring exemptions
- Life insurance creates tax-free liquidity, which can help offset lack of step-up in basis on assets in trust

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## By the Numbers

| YEAR    | SALE AMOUNT (DISCOUNTED) | INTEREST PAID* 1.15% | GIFT    | APPROXIMATE PREMIUM | ASSET VALUE @2% (EOY) | CASH in TRUST (EOY) | DEATH BENEFIT | NET TO HEIR FROM TRUST NET of NOTE |
|---------|--------------------------|----------------------|---------|---------------------|-----------------------|---------------------|---------------|------------------------------------|
| 1       | 5,600,000                | 64,400               | 560,000 | (384,895)           | 8,160,000             | 717,709             | 30,000,000    | 33,277,709                         |
| 5       |                          | 64,400               | 0       | (384,895)           | 8,832,646             | 1,541,573           | 30,000,000    | 34,774,220                         |
| 10      |                          | 64,400               | 0       |                     | 9,751,955             | 3,487,596           | 30,000,000    | 37,639,551                         |
| 15      |                          | 64,400               | 0       |                     | 10,766,947            | 8,011,125           | 30,000,000    | 43,178,072                         |
| 20      |                          | 64,400               | 0       |                     | 11,887,579            | 13,943,165          | 30,000,000    | 50,230,744                         |
| 25      |                          | 64,400               | 0       |                     | 13,124,848            | 21,633,467          | 30,000,000    | 59,158,315                         |
| 30      |                          | 64,400               | 0       |                     | 14,490,893            | 31,512,203          | 30,000,000    | 70,403,096                         |
| 35      |                          | 64,400               | 0       |                     | 15,999,116            | 44,107,865          | 30,000,000    | 84,506,982                         |
| 37 (LE) |                          | 64,400               | 0       |                     | 16,645,481            | 50,047,555          | 30,000,000    | 91,093,036                         |

Estate tax savings = \$36M+

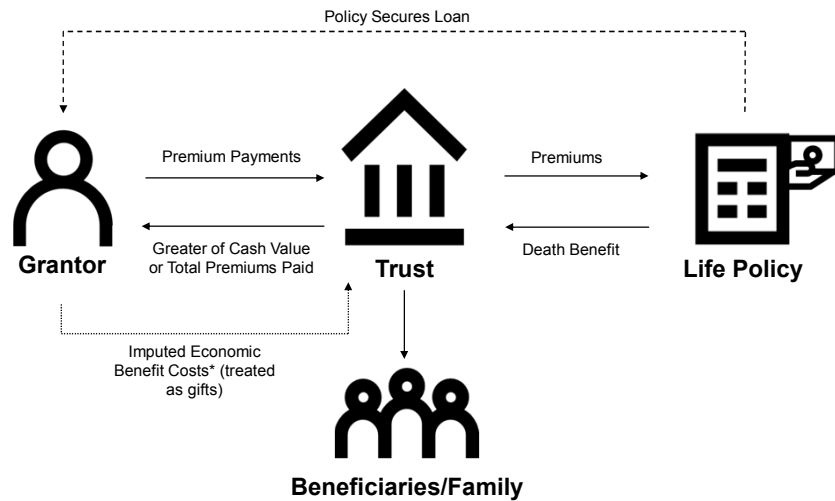
\*Cash in trust includes 7.5% cash flow from non-discounted asset, 4% return on side fund (cash), minus expenses (premiums & interest)  
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## Private Split Dollar



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\*\*Determined based on net amount of DB payable to the trust each year, economic benefit rates (Table 2001 or carrier alternative term rates), and insured's age  
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## Structuring the Private Split Dollar

- Mr. Smith (Grantor) creates ILIT for the benefit of wife and children; independent trustee appointed
- Grantor pays yearly premium in return for right to be repaid "greater of cash value or premiums paid"
- Approximate Yearly Premium = \$384,895
- No interest payments – instead "economic benefit" paid via gifts
- Exit strategy = Grantor-funded GRAT
- \$8,365,732 of securities/liquid investments transferred to 10-year GRAT
- Annual annuity payment = \$873,824
- Expected remainder = \$3,464,055

### Benefits

- Uses economic benefit rates vs. interest rates
- Makes it easy to get policy in force without having to transfer assets other than premium
- Flexible to use with many exit strategies

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## By the numbers

| YEAR | APPROXIMATE PRIVATE SPLIT DOLLAR PREMIUM | CASH SURRENDER VALUE | SPLIT DOLLAR AMOUNT DUE | ANNUAL GIFTS (ECONOMIC BENEFIT) | SIDE FUND (GRAT REMAINDER) | DEATH BENEFIT | NET TO HEIRS |
|------|--|----------------------|-------------------------|---------------------------------|----------------------------|---------------|--------------|
| 1    | 384,895                                  | 0                    | 384,895                 | 713                             | -                          | 30,000,000    | 29,615,105   |
| 2    | 384,895                                  | 74,087               | 769,790                 | 850                             | -                          | 30,000,000    | 29,230,210   |
| 3    | 384,895                                  | 305,361              | 1,154,685               | 1,001                           | -                          | 30,000,000    | 28,845,315   |
| 4    | 384,895                                  | 553,495              | 1,539,580               | 1,174                           | -                          | 30,000,000    | 28,460,420   |
| 5    | 384,895                                  | 876,083              | 1,924,475               | 1,388                           | -                          | 30,000,000    | 28,075,525   |
| 6    | 384,895                                  | 1,220,633            | 2,309,370               | 1,678                           | -                          | 30,000,000    | 27,690,630   |
| 7    | 384,895                                  | 1,583,600            | 2,694,265               | 2,072                           | -                          | 30,000,000    | 27,305,735   |
| 8    | 384,895                                  | 1,966,768            | 3,079,160               | 2,614                           | -                          | 30,000,000    | 26,920,840   |
| 9    | 384,895                                  | 2,372,024            | 3,464,055               | 3,337                           | -                          | 30,000,000    | 26,535,945   |
| 10   | 0  | 2,484,181            | (3,464,055)             | 4,304                           | 3,464,055                  | 30,000,000    | 30,000,000   |

**Cumulative Gifts = \$19,129**

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## Comparison of Options

|                         | Gifts           | Private Loan    | Sale to Trust*              | Private S/D         |
|-------------------------|-----------------|-----------------|-----------------------------|---------------------|
| Death Benefit           | 30,000,000      | 30,000,000      | 30,000,000                  | 30,000,000          |
| Premium (9 pay)         | 3,464,055       | 3,464,055       | 3,464,055                   | 3,464,055           |
| Upfront Asset Transfer  | 11,580,000      | 7,527,467       | 5.6M discounted + seed gift | 8,365,732 (GRAT)    |
| Asset Type              | Cash/Securities | Cash/Securities | Commercial RE               | Cash/Securities     |
| Term of Transaction     | -               | 9               | 9                           | 10                  |
| Interest Received       | -               | 392,931         | 579,600                     | 8,738,241 (annuity) |
| TOTAL Gifts             | 11,580,000      | -               | 560,000                     | 19,129              |
| TOTAL AMOUNT RETURNED** | -               | 7,920,398       | 6,179,600                   | 12,202,296          |

\*For purposes of comparison, assume promissory note is repaid with cash/assets beginning of Year 10.

\*\*Includes repayment obligation & interest paid

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# Questions?



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Insurance policies and/or associated riders and features may not be available in all states.

Loans and withdrawals will reduce the death benefit, cash surrender value, and may cause the policy to lapse. Lapse or surrender of a policy with a loan may cause the recognition of taxable income. Policies classified as modified endowment contracts may be subject to tax when a loan or withdrawal is made. A federal tax penalty of 10% may also apply if the loan or withdrawal is taken prior to age 59 1/2. Insurance products are issued by John Hancock Life Insurance Company (U.S.A.), Boston, MA 02216 (not licensed in New York) and John Hancock Life Insurance Company of New York, Valhalla, NY 10595.

Trusts should be drafted by an attorney familiar with such matters in order to take into account income and estate tax laws (including the generation-skipping tax). Failure to do so could result in adverse tax treatment of trust proceeds.

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