

LEVERAGING ANNUAL EXCLUSION GIFTS WITH LIFE INSURANCE

Maximizing annual exclusion gifts with the purchase of life insurance in an irrevocable trust significantly increases the amount of wealth received by a donor's heirs free of income and transfer taxes.

Mama Leone is a 68-year-old widow; she and her husband were successful restaurateurs and owned a number of commercial properties. She is in good health and has five children and 11 grandchildren. Her overall estate is worth \$25 million.

HOW GIFTING WITH LIFE INSURANCE WORKS

Mama Leone hates paying taxes nearly as much as she loves the church and she would like to leave her estate to the church so that she doesn't have to pay any estate taxes. The problem is that she's worried about not leaving enough to her kids and grandkids. But now she's got a plan! Mama Leone going to leave \$11.9M to her heirs (because that's estate tax free under federal law and the rules of portability) and \$13.1M to the church. Then, she's going to take her attorney's advice to start making annual exclusion "Crummey" gifts and create an irrevocable trust. With 16 potential Crummey beneficiaries, Mama Leone's gifting budget is \$224,000 per year (16 x \$14,000). By using annual exclusion gifts, Mama Leone won't have to dip into her lifetime gift tax exclusion. She will, however, apply her federal generation-skipping transfer (GST) exemption to each Crummey gift so that her trust can be a dynasty trust.

Mama Leone's attorney also recommends that she apply her gift budget toward the purchase of a policy on her life to provide estate tax liquidity upon her death. In her case, an annual premium of \$224,000 will purchase a policy with a death benefit of approximately \$10.2 million.

Upon Mama Leone's death, the trust will receive the insurance death benefit free of income and transfer taxes. The \$10.2 million death benefit will be invested in the trust for the benefit of the children, grandchildren and Mama Leone's future descendants.

BENEFITS OF THE PLAN

- At Mama Leone's death, the trust will receive the insurance death benefit free of income and transfer taxes.
- The \$10.2M death benefit will be combined with the \$11.9M that her heirs will receive outright.
- Mama Leone won't pay any gift taxes as she makes the annual gifts to the trust.
- At her death, the trust will receive In addition, the church will receive the \$13.1M remaining in her estate.
- In addition, the church will receive the \$13.1M remaining in her estate — allowing her to avoid paying transfer taxes, leave heirs \$22M and leave a sizeable legacy to charity.

If Mama Leone had not decided to implement this plan, she would have left \$19.76M to her kids and paid \$7.86M in estate taxes. By utilizing the power of annual gifting, charitable estate tax deductions, and life insurance, Mama Leone was able to save in taxes, leave more to her kids and still benefit charity.

Not invested in insurance are assumed to grow at 3 percent net.

BENEFITS OF GIFTING WITH LIFE INSURANCE

Life insurance provides valuable estate liquidity at death.

- Assets inside the trust are protected from the reach of creditors, providing asset protection for the family.
- Any assets gifted to the trust can be leveraged free of gift, estate and GST taxes.
- The policy death benefit is received by the trust free of income and estate taxes.
- The trust can be structured to be a dynasty trust, with all trust assets exempt from the federal GST tax.

CONSIDERATIONS OF GIFTING WITH LIFE INSURANCE

- Donor loses access to the assets transferred to the trust.
- There are annual trust administration and gift tax return costs.
- Trust must be carefully drafted to provide for Crummey gifts, proper allocation GST exemption and asset protection.

THE BOTTOM LINE

Maximizing annual exclusion gifts with the purchase of life insurance in an irrevocable trust significantly increases the amount of wealth received by a donor's heirs free of income and transfer taxes. And if the trust is structured as a dynasty trust, the donor can provide a legacy for future descendants.

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