Manulife Financial

ADVANCED MARKETS

Concept Profile

THE POWER OF LIFETIME GIVING

It is often said that it is better to give than to receive. In the case of estate planning, this adage is often true. Establishing a lifetime gifting program is an excellent way to reduce the impact of estate taxes.

WHAT IS A GIFTING PROGRAM?

A lifetime gifting program is when a person uses his or her annual exclusion gifts to transfer money from his or her estate to someone else. This is the easiest way to reduce the size of an estate and the impact of estate taxes. This type of program can also be established between a person and an irrevocable life insurance trust.[1]

WHAT IS AN ANNUAL EXCLUSION GIFT?

Each person is allowed to make annual gifts up to $10,000 per person without having to pay gift tax. These gifts, known as annual exclusion gifts, are an excellent way to reduce the size of an estate at no additional cost.

HOW DOES A GIFTING PROGRAM WORK?

There are many ways to set up a gifting program. The simplest way is to give money to the beneficiary and then he or she can do with it as they wish. However, a more effective and lucrative way to set up a gifting program is to gift the money to an irrevocable trust. By gifting to an irrevocable trust, the money is removed from the taxable estate and the proceeds can be used at the death of the trust grantors to pay estate tax or other expenses at death.

To implement a gifting program the donors can use both their annual exclusions and their applicable exclusion amounts to make gifts to the trust.[2] The trustee will determine the trust investments or can use the proceeds to purchase a life insurance policy on the lives of the donors.

EXAMPLE

Sean and Kelley MacCauley are both age 55 and have an estate worth about $10 million. Recently, they concluded that they needed to start putting an estate plan into place. They met with their advisor who recommended that they establish a gifting program. He recommended that they create an Irrevocable Life Insurance Trust (ILIT). By doing this, Sean and Kelley will not only reduce their exposure to estate taxes, but will also have a fund outside of the taxable estate that their children may use to pay any expenses that occur at their death.

Sean and Kelley have two children and two grandchildren. They are going to gift $80,000 each year to the ILIT free of gift tax. The trustee of the ILIT will buy a survivorship life insurance policy with a death benefit of $10,236,329 on the lives of Sean and Kelley. At the second spouse's death, the beneficiaries of the trust will inherit the insurance proceeds free from estate and income taxes and will have the option of using these proceeds to pay any additional estate expenses.

WHY ESTABLISH AN ILIT?

Some people are reluctant to establish a gifting program with an irrevocable life insurance trust. However, an ILIT is an excellent vehicle to leverage a gifting program. A life insurance policy has:

- **Tax deferred accumulations:** Potential cash value inside of a life insurance policy grows income tax-deferred. Thus, a gifting program that uses an ILIT can make distributions to trust beneficiaries during the lives of the insureds.
- **Income–tax free death benefit:** In addition to being free from estate taxes, the death benefit of a life insurance policy owned by an ILIT passes to the heirs free from income taxes.[3]
- **Tax-favored distributions:** Distributions from a life insurance policy are income tax-free up to the policy cost basis.[4]

SUMMARY

A gifting program is an excellent way to reduce the size of your estate. A gifting program that includes an ILIT is an excellent way to maximize the amount that is passed to heirs.

For more information about the power of lifetime giving, please contact your local Manulife Financial Representative or call the Advanced Markets Group at (888) 266-7498, option 3.

1 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.

2 The annual exclusion amount in 2001 is $10,000 per person. CCH Inc. (Commerce Clearing House) has projected that the annual exclusion amount will increase to $11,000 in 2002. Although this is not the official number from the IRS, the projection is based on the CPI (Consumer Price Index) rate for the fiscal year that ended on August 31, 2001.

3 Life insurance death benefit proceeds are generally excludable from the beneficiary's gross income for income tax purposes. There are a few exceptions, such as when a life insurance policy has been transferred for valuable consideration. No legal, tax or accounting advice can be given by Manulife Financial, its agents, employees or registered representatives. Prospective purchasers should consult their professional tax advisor for details.

4 Withdrawals and loans from life insurance policies which are classified as modified endowment contracts may be subject to tax at the time the withdrawal or loan is made. A federal tax penalty may also apply if the withdrawal or loan is taken prior to age 59 1/2. Withdrawals and loans also have the effect of reducing the death benefit and cash surrender value and may cause the policy to lapse. Lapse of a life insurance policy can cause the loss of death benefit and adverse income tax consequences.

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