CAPITAL STRATEGIES

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M INTELLIGENCE

LIFE INSURANCE ENHANCES PLANNING WITH SLATS

Dual spousal lifetime access trusts (dual SLATs) offer couples a tremendous opportunity to ensure financial security today and transfer substantial wealth to a dynasty trust. Life insurance planning can enhance the benefits and financial security provided by dual SLATs.

BACKGROUND

Clients who can afford to make sizable gifts have a tremendous, though time-sensitive, planning opportunity. In 2023, the individual gift/estate and generation-skipping tax (GST) exemptions increased to $12.92 million ($25.84 million for a married couple), and lifetime exemptions will be indexed for inflation. However, this opportunity may be short-lived. The current law sunsets at the end of 2025, halving the exemption starting in 2026. And there may be an even more daunting challenge. Many clients are unwilling to make sizable gifts because they are unwilling to give up access to and control of substantial assets.

Enter dual spousal lifetime access trusts (dual SLATs).[1] With dual SLATs, each spouse creates a trust for the benefit of the non-grantor spouse, children, and future generations funded with the grantor's lifetime exemption gifts. Dual SLATs move assets into a dynasty trust that avoids repeat estate taxation for generations and allows the "marital unit" (spouses) to retain access to and control of those gifted assets as long as both spouses are alive. There is, however, a downside: at the first death, the surviving spouse loses direct access to and control of half the assets — those in the trust they created.

When considering dual SLATs, it's important to address the reciprocal trust doctrine which states that if the two SLATs are too similar, SLAT assets could be included in the spouses' estates. As a result, it's important that the dual SLATs have sufficient differences.[2]

LIFE INSURANCE PLANNING WITH DUAL SLATS

Life insurance is a powerful tool that can complement and enhance SLAT planning. Consider the following strategies:

1. Single Life Insurance Policies (vs. Survivorship Life)
2. Stacking Gifts
3. The Triple Trust Solution

We'll use a case study to explore these powerful strategies.

Assume that we have a husband and wife, ages 65 and 60, with a successful business and an estimated estate tax liability of $25 million. You have been working with them recently and have recommended the following estate planning strategies:

- A revocable living trust with a pour-over will to replace their outdated wills and update core documents.[3]

- Annual exclusion gifts to adult children.[4]
- Dual SLATs where each spouse creates a trust for the benefit of the non-grantor spouse, children, and future generations funded with $12.92 million lifetime exemptions ($25.84 million combined).[5]
- An irrevocable life insurance trust (ILIT) to own $25 million of survivorship life for the benefit of children and future generations.

1. SINGLE LIFE INSURANCE (VS. SURVIVORSHIP LIFE)

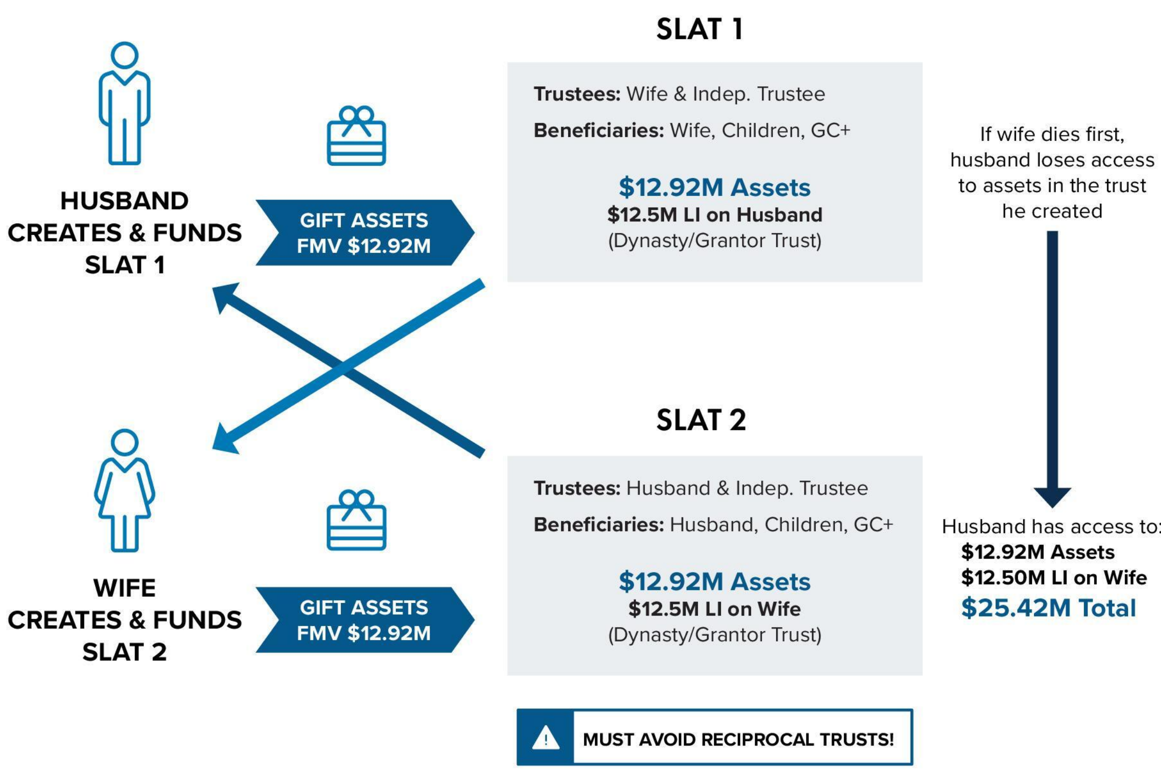
The clients like the proposed plan and are interested in beginning implementation. However, upon learning that on the first death the surviving spouse loses direct access to the $12.92 million in the SLAT, the clients start to cool on the plan. Without missing a beat, as an alternative to the $25 million of survivorship life, you recommend that each SLAT purchases $12.5 million of permanent life insurance on the life of the grantor with premiums paid from the cash flow from the $12.92 million of assets and, as lifetime exemptions increase, from future gifts. In other words, the husband's trust owns $12.5 million of coverage on his life for the benefit of his wife and other trust beneficiaries and vice versa with respect to the wife's trust.[6]

The clients buy into the plan appreciating that:

1. While both spouses are alive, they have access to and control of the $25.84 million of gifted assets.
2. The surviving spouse benefits from the insurance replacing the assets that he or she can no longer access.

   For example, if the wife dies first, the husband loses access to the $12.92 million of assets in the trust he created, but he has access to assets in the SLAT created by wife: i) $12.92 million of gifted assets and ii) $12.5 million of death from the policy insuring the wife. In essence, the life insurance makes him whole with combined access to and control of $25.42 million of assets.
3. They don't have to make additional gifts to fund the life insurance.
4. They don't have to create and fund a survivorship ILIT.
5. Ultimately, the $25 million of combined death benefit coverage will be available in a dynasty trust to pay estate taxes.

Single Life Insurance in Each SLAT



2. STACKING GIFTS

Over time as your conversations proceed, the clients' business experiences a slow-down, and they get nervous about gifting $25.84 million. They balk at the cost of the two single life policies for $12.5 million of insurance on each spouse which cost 60% more than $25 million of survivorship coverage. They decide that they are comfortable gifting one full exemption equal to $12.92 million split equally between the two SLATs. You explain that, if each spouse gifts $6.46 million to a SLAT and the current gift/estate and GST exemptions "sunset" (get cut in half) as scheduled on December 31, 2025, they will each have lost $6.46 million of "bonus exemption" (the amount of exemption scheduled to lapse = half of $12.92 million) and future appreciation of the unused or wasted gift opportunity.

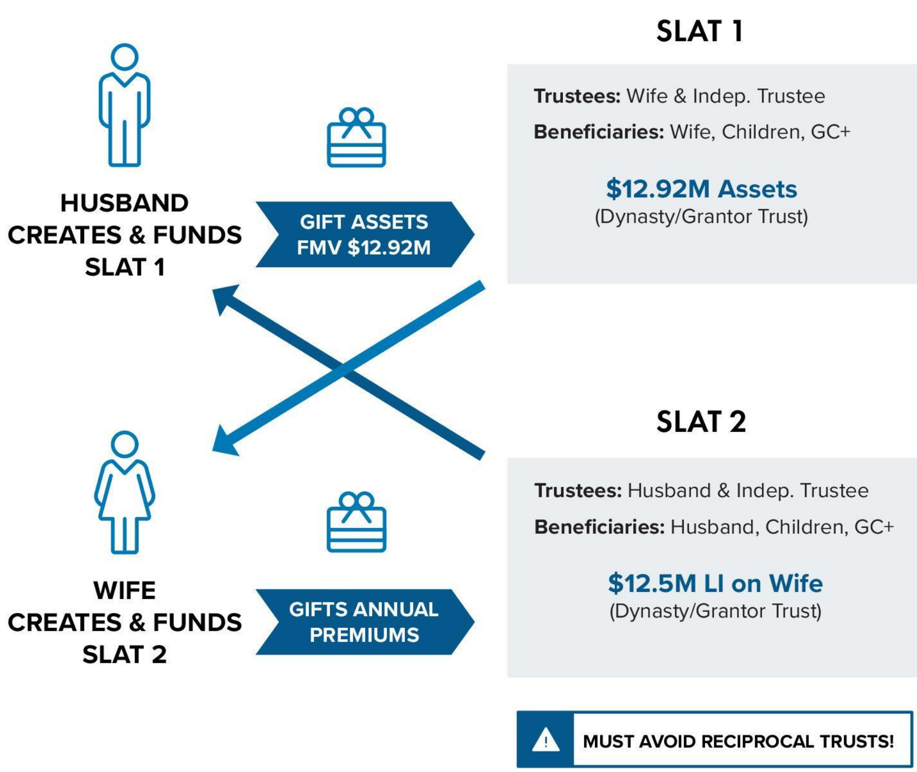
You suggest that there is a better approach, recommending that they "stack gifts" by creating and funding dual SLATs as follows:

- The husband creates a SLAT for the benefit of the wife and future generations and gifts his full $12.92 million lifetime exemption.
- The wife creates a SLAT for the benefit of the husband and future generations funded solely with $12.5 million of life insurance on the wife's life.[7]

By stacking gifts, the clients have preserved the husband's full exemption and, assuming sunset in 2025, half of the wife's exemption.

If the husband dies first, his wife has access to the $12.92 million of assets in the SLAT he created. If the wife dies first, the SLAT she created receives $12.5 million of death proceeds that can be used to provide for him. These insurance proceeds can be invested by the wife's SLAT or used to purchase assets from the estate at the first or second death. Importantly, the couple has preserved at least three-quarters of their lifetime exemptions: the husband has used his full lifetime exemption while the wife has retained at least half of hers (in the event of "sunset"). And all of this has been accomplished in dynasty trusts!

Stacking Gifts with Life Insurance



3. THE TRIPLE TRUST SOLUTION

As underwriting proceeds, the clients' business rebounds, and they decide that they are comfortable funding each SLAT with $12.92 million of assets ($25.84 million combined). With the SLATs fully funded, they decide the single life coverage on each is unnecessary. They agree that $25 million of survivorship life insurance in its own ILIT is needed to protect the business and keep it in the family.

They appreciate the creative life insurance solutions, but do not want to be personally bound to the ongoing funding of the survivorship life insurance. They ask if the cash flow from the SLATs' assets can be used to fund the survivorship life insurance.

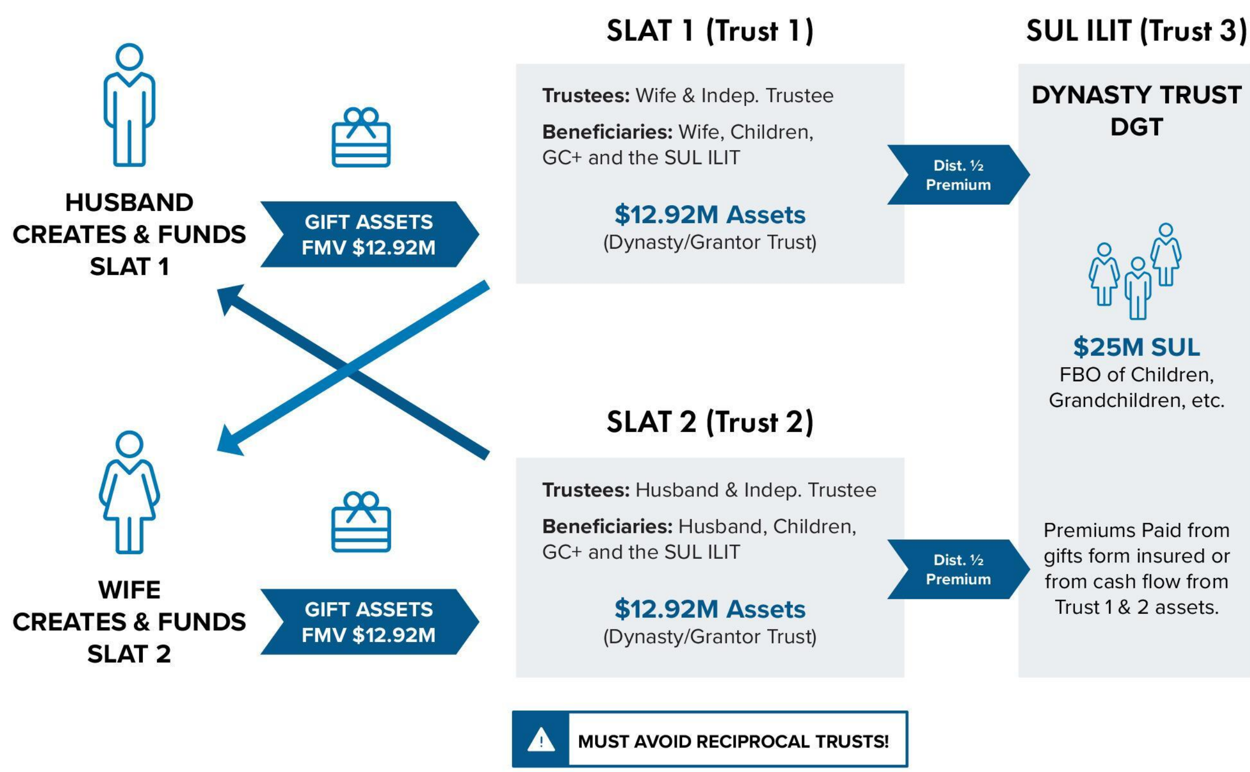
You introduce the "triple trust solution." The SLATs have not yet been executed so that it is not too late to make the survivorship ILIT a permissible beneficiary of each SLAT. As a result, either SLAT can distribute excess cash flow to the survivorship ILIT to pay policy premiums. Of course, if they choose to, they are still free to make direct gifts (for example, as exemptions increase) or use other funding strategies such as split-dollar advances or loans. Although there are possible combinations of GST exempt and non-exempt trusts, best practice is to ensure that all three trusts are fully GST exempt.

The triple trust solution offers another benefit following the first death. Suppose that while both spouses are alive, the two SLATs are splitting a $250,000 annual premium with each contributing $125,000 to the survivorship ILIT. If the husband dies first, the wife loses access to the assets in the SLAT she created. An elegant solution would be to pay the full $250,000 premium from the SLAT she created, preserving the greater SLAT 1 income to provide for her.

DUAL SLATS GIVE CLIENTS MANY PLANNING CHOICES

In closing, there are many iterations of these strategies. For example, the stacking gifts strategy using single life coverage on one spouse could be combined with the triple trust solution for survivorship life. Or term insurance owned by the SLAT created by the insured may be introduced to the triple trust solution to provide income protection for a limited duration. For some clients, SLATs that only use life insurance may be attractive. The good news is that while every case has its unique challenges, each has its unique solutions. Creative thinking will serve clients well by providing a solution that protects their present and future financial well-being and gives them peace of mind.

The Triple Trust Solution



This piece was created by M Financial's Advanced Markets experts and produced by the marketing team.

[1] See "The Benefits of a SLAT: Efficiency and Access" (M Intelligence) for a detailed discussion of SLATs.

[2] Reciprocal trusts are easily avoided. To break reciprocity, the trusts can be created and funded at different times with different assets, have different dispositive provisions (income and principal, one beneficiary spouse holds a 5x5 power) with different timing, or be formed in different states (NV and SD) with different independent trustees.

[3] Core documents include a living will, health care proxy, and durable power of attorney.

[4] $17,000 per donor per donee in 2023. For example, a husband and wife with three children can gift $102,000.

[5] Lifetime exemptions, currently equal to $12.92 million per individual (2023), consist of gift/estate and generation skipping transfer tax (GST) exemptions. The gift and estate exemptions are "unified" in that to the extent that the gift tax exemption is used during lifetime, both the gift and estate exemptions are reduced.

[6] If clients aren't ready to make any substantial gifts, the dual SLATs could be initially funded only with life insurance. Later, as their comfort level improves, the clients could make gifts to the SLATs. And, as discussed in endnote seven, the amount of insurance is flexible. For example, the clients might place $5 million of coverage on each grantor and $15 million of survivorship life.

[7] The amount of life insurance on the insured's (wife's) life is flexible and should be tailored to the clients' goals and objectives. One alternative is to fund the amount in the husband's SLAT, for example, $12.92 million, the amount husband gifted to the SLAT he created. Another alternative would be to place $10 million on the wife's life.

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