Life Insurance for Estate Planning Purposes with Access to Cash Values for Lifetime Needs

Many individuals will purchase a single life policy to provide income protection for their family, funds for estate taxes or cash to equalize inheritances among children. For high net worth individuals, however, if you own the policy outright, the death benefit may be subject to estate taxes. To remove the death benefit from your gross estate, many estate planners recommend that insurance be owned in an irrevocable life insurance trust (ILIT). An ILIT is an irrevocable trust that is the owner and beneficiary of a life insurance policy. The trust cannot be amended or revoked. That, however, may prevent you from accessing the policy's cash values for use during your lifetime. That is a frequent source of concern causing indecision around implementing an ILIT.

One Solution: Spousal Limited Access Trust

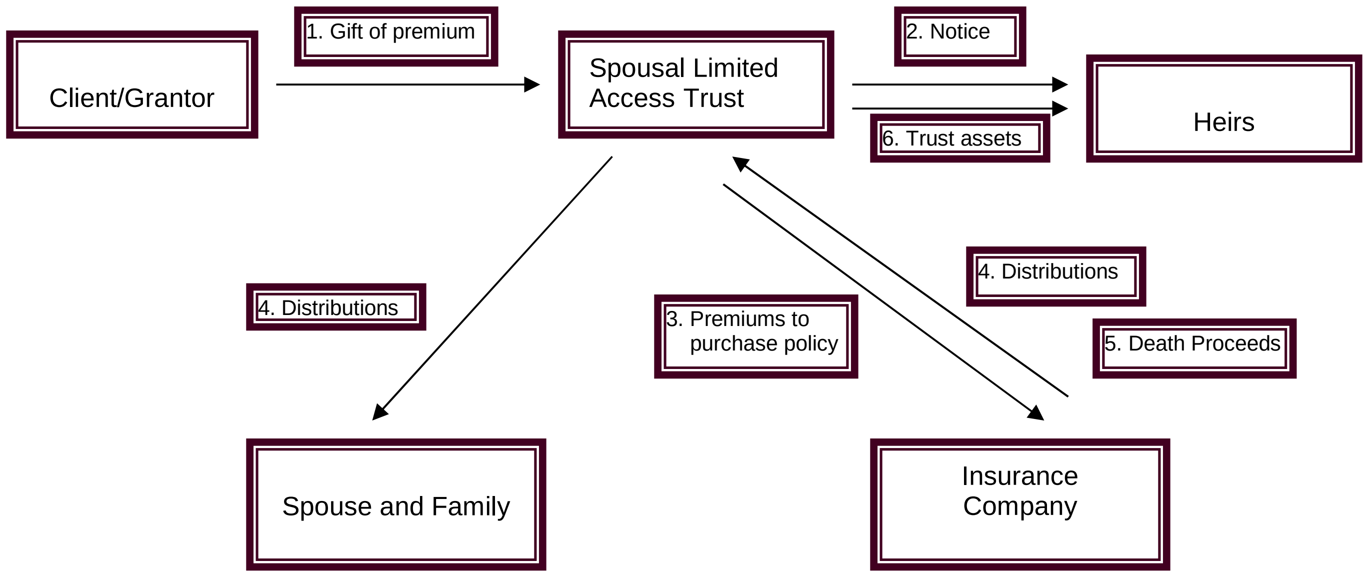
A life insurance policy has the potential to accumulate significant cash value during your lifetime which may be unavailable to you and your family if the policy is locked into an irrevocable trust. By law, if you can access the policy cash values, then the death benefit will be included in your gross estate. That would not be a good outcome for high net worth individuals.

A Spousal Limited Access Trust (SLAT) may, however, give you access to cash values (indirectly through your spouse) while also keeping the life insurance proceeds out of your taxable estate.

The strategy is simple to implement. A SLAT is nothing more than an ILIT that contains provisions allowing trust assets to be used for the benefit of your spouse and children. Your spouse can even be the Trustee. You make a gift of the life insurance premium to the trust, and the Trustee applies for and is the owner and beneficiary of a life insurance policy on your life. The trust provides that discretionary distributions can be made to your spouse and children during your lifetime, typically for their health, education, maintenance and support. If you name a "disinterested" trustee (other than your spouse or someone with an interest in the trust) even more liberal discretionary distributions can be made by the Trustee. Distributions are made by taking withdrawals from or taking loans against the policy.

Note, however, that taking loans and withdrawals from the policy can reduce the death benefit and impact your estate plan. In addition, unless properly provided for in the trust document, or addressed by state law, a divorce can ruin the best of plans.

How Does It Work?



1. Joe needs life insurance to protect his wife and three children at his death. He would also like to save more for retirement, over and above his qualified retirement plans. He is considering purchasing a cash value policy in order to supplement his retirement income but he also knows that he has estate tax exposure upon death. His financial advisor recommends that he implement a Spousal Limited Access Trust because if he owns the policy himself, he can freely access the cash value but the death benefit would be included in his taxable estate.
2. With the assistance of Joe's estate planning attorney, the SLAT is created and he gifts the amount of the premium each year to the trust. The attorney instructs Joe on some of the technical requirements in making the gift to ensure that Joe leverages his exemptions for gift taxes, one of which includes providing notice of the gift to the beneficiaries of the trust.
3. The trustee purchases and owns the life insurance on Joe's life and makes the premium payments.
4. As cash values build up over the years, the trustee may make distributions to Joe's spouse and family members, if needed, by withdrawals up to the amount paid in, or loans against the policy.
5. Upon Joe's death, the insurance proceeds will be paid to the trust.

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6. The trust assets can continue to be held in trust for the benefit of Joe's family or distributed to them.

Advantages

- Provides additional estate planning flexibility by permitting the trustee to access the policy values for the benefit of the beneficiary spouse and family in the event of changes in the estate tax laws, or financial need of the family.
- Cash values may be distributed from the policy on a tax favorable basis during your lifetime through withdrawals and/or policy loans.*
- Cash values can be used as an indirect source of supplemental retirement income.
- The death benefit payable to the trust upon your death will be excluded from your gross estate.
- Trust assets can be retained in trust and passed on to your heirs estate tax-free or used on their behalf, protected from creditors.

*****Policy benefits are reduced by any outstanding loan or loan interest and/or withdrawals. Dividends, if any, are affected by policy loans and loan interest. Withdrawals above what is paid into the policy may cause ordinary income taxes to be paid on the gain portion of the policy. If the policy lapses, any withdrawals or loans considered gain in the policy may be subject to ordinary income taxes. If the policy is a Modified Endowment Contract (MEC), loans are distributed like withdrawals. All withdrawals are distributed as gain first and subject to ordinary income taxes. If the insured is under 59 1/2 the gain portion of the withdrawal is subject to a 10% tax penalty.

Please consult with your Guardian Financial Representative if you have any questions concerning this document.

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GEAR #2011-12020 Expiration: 6/30/2016

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