as we see it

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THOUGHTS FROM OUR CHAIRMAN

In this issue, our associate, Ted Staples reviews an estate planning option which can provide tax-sheltered extra cash at death.

The current investment climate has its challenges. The headlines pertaining to slowing global growth, trade, interest rates, politics and the saber rattling in the Middle East and Pacific Rim are contributing to market volatility. The dollar amounts of these swings are substantial but we have not yet experienced the long anticipated bull market correction of 8 to 10%. Some believe the equity market in the USA has in the last six months been "climbing a wall of worry." It has also been suggested that we could be talking ourselves into a recession. Fortunately, however, the US consumer seems to be comfortable. We are spending more and saving more. On the other hand, the headline issues are causing concern amongst company leaders. Many are holding back on capital investments in their businesses as they wait to see what effects these global issues will have on consumers and the general business climate. When economic slowdown occurs with accompanying market weakness it could present good, long term investment opportunities. In the meantime, we are looking to take advantage of small corrections to put modest cash reserves to work and are ever mindful of important volatility measures such as *beta* for equity holdings.

Alfred B. Van Liew

Is an ILIT for You?

Edward K. Staples

The story goes that a trustee is advising a client about asset leveraging and a liquidity need in their eventual estate.

"John, how about I give your attorney a call? Based on our discussion today, I think you are a strong candidate for an Irrevocable Crummey Trust."

Looking up somewhat quizzically, John nods affirmatively,

"Okay, thanks…but, a 'Crummey Trust'? Can't I get one that's not set in stone with a more reassuring name?"

"ILIT" is the acronym for an Irrevocable Life Insurance Trust. The Crummey "tag" refers to a court decision (*Crummey et al v. Commissioner of Internal Revenue, Cir.1968*) whereby gifts to a life insurance trust for premium payments can be excluded from US gift tax assessments. When the creator (grantor) of the trust makes a "gift" to the trust of a premium payment, a Crummey letter conforming to criteria under the law is prepared by the trustee to formally notify the trust beneficiaries of receipt of the payment. Under the trust provisions they are given a brief window (typically 30 days) in which to withdraw their pro rata portion of the premium addition. They should be made aware that the future benefit - the insurance payout - far outweighs the receipt of a share of a premium payment.

The reason the trust is written as *irrevocable* is so that as a policy purchased and owned by the trust, it is held in an entity with a separate tax identification number. That way there is no incidence of ownership or control by the grantor other than the allowance for them to make recurring premium payments and select objective trustees. This keeps the trust – and it's death benefit – outside of the grantor's estate for income and estate tax purposes. The leveraging aspect of an ILIT is simply that by current payment of a relatively small premium there will be a large untaxed death benefit available when the need arises.

What happens when the grantor (or co-grantor for a second to die insurance plan) passes away? There are a number of planning benefits achieved by the establishment of a trust, and they carry out to ILITs. Life insurance proceeds are often used to fill anticipated or unanticipated funding needs in estate plans. For example, a family business might have intrinsic value, but lack the current cash flow to cover expenses and keep things running at the passing of a principal. Rather than being forced to liquidate assets or institute a hasty distress sale, the death benefit supplied by the ILIT could provide temporary relief until better sale prospects or retention efforts are afforded.

Depending upon your overall goals, the trust may be managed for a beneficiary's future needs or terminate by outright distribution of the property. Regardless, an important feature of trusts is the retention of prudent control over the disposition of assets by the trustee. Legally entrusted to follow your wishes as stated in the trust document, the trustee may employ discretionary language of the trust document allowing for a "second look" when making important decisions in support of beneficiaries. If a beneficiary is the recipient of state and/or federal disability benefits, for example, the trustee may opt to accumulate funds rather than make distributions which could negatively impact the beneficiary's qualification for those benefits. The trustee's consideration of such contingencies – viewing each beneficiary's circumstances on a case by case basis – may also aid in the reduction of income taxes for those who are at a higher marginal income tax rate.

Another positive aspect of trusts is that the assets are excluded from matters regarding the probate court. This effectively eliminates public disclosure of the assets, saves on legal and court costs and reduces the likelihood of delay in accessing the property to support the beneficiaries. Additionally, since the assets are registered to the trust and not directly owned or controlled by the grantor and beneficiaries, there is an extra layer of asset protection against personal liability and potential creditor claims.

How do you get started? After consulting with your trustee and other advisors to determine if an ILIT would be appropriate in your overall estate plan, first make sure that you qualify for the appropriate insurance policy. As noted previously, it is crucial that the policy be purchased *by the trust* after the document is drafted by your attorney. Weigh the initial and ongoing administrative costs of instituting the plan versus having the life insurance proceeds paid directly to your family and/or business. Lastly, you and your trustee may choose to educate the beneficiaries about the workings of the plan for the best financial outcome.

An ILIT – especially a Crummey one – isn't for everyone. But it may just be a key piece of your planning for the future offering asset protection, a shot of liquidity at an opportune time and the leveraging of your current asset mix.