



Untrustworthy Beneficiaries: Avoid Crummey Withdrawal Powers - Use Gift Tax Applicable Exclusion Amount

Prospects are often hesitant to commit to an irrevocable life insurance arrangement for one or more of the following reasons:

- They are already using their gift tax annual exclusion amount to make gifts to family members.
- Family members currently receiving gifts don't want to see those gifts redirected to pay life insurance premiums.
- Parents feel that their children can't be trusted to waive their Crummey withdrawal rights and that they will take gifts out of the trust when given the opportunity.

If you have run into any of these problems, you may want to consider the following solution.

FACTS: Paul and Helen have a \$10 million estate. They have three children, Diana, Mary and Joe. Diana has her own successful business. Unfortunately, Mary and Joe have had problems. Mary is employed and married but she and her husband have built up large credit card debts and are struggling financially. Meanwhile, Joe has a substance-abuse problem.

Paul and Helen want to fund an irrevocable life insurance trust with annual cash gifts, but they are concerned that if Mary and Joe receive notice that they can withdraw their share of the gifts, they will do so, and defeat the funding of the trust. Fortunately, there is a way to avoid giving the children Crummey withdrawal rights and still avoid paying gift taxes on the transfers. Here is how it works.

SOLUTION: It is possible to transfer premium payments to a life insurance trust without subjecting the gifts to Crummey withdrawal powers and still avoid paying gift taxes on the transfer by using the gift tax applicable exclusion amount.

The Economic Growth and Tax Relief Reconciliation Act of 2001 increased the gift tax applicable exclusion amount to \$1 million. This means an individual can transfer \$1 million of property during his/her lifetime without paying gift taxes. This amount is in addition to the \$12,000 gift tax annual exclusion (2006 amount, indexed for inflation). Unlike the gift tax annual exclusion, transfers using the gift tax applicable exclusion do not require the trust beneficiaries to have an unrestricted right to access the transferred property. That

means that the beneficiaries cannot withdraw money that was earmarked to pay life insurance premiums from the trust.

Either Paul or Helen (or both) can use their gift tax applicable exclusion amount to fund the trust. We have assumed that Paul has decided to use his and has gifted \$1,000,000 to an irrevocable life Insurance trust (ILIT), which will purchase a PruLife® SUL Protector policy on Paul and Helen. See the illustration that follows for the results. (The insurance amount could double if Helen also used her \$1,000,000 exclusion.)

The children will have no withdrawal rights to the trust. The gifts will be future interest gifts, but they will be free of gift tax up to the exclusion amount. The amount of estate tax applicable exclusion available at Paul's or Helen's death will be reduced by the amount of the gifts they used during their lifetime.

Paul and Helen can accomplish their goal of estate protection while alleviating their concern that their funding plan might be undermined by their children. And they will have flexibility in structuring their gifts to the trust.

PruLife® SUL Protector is well suited to meet the objectives of this concept. For clients who desire guarantees and premium flexibility, this product offers a flexible premium design that can accept a large single premium payment that will provide a lifetime death benefit guarantee¹. For clients that prefer to spread payments over several years, our 'No-Lapse Guarantee' illustration solve will calculate a premium that can be paid over ANY number of years that will provide a lifetime guarantee of the initial death benefit.

SAMPLE LEDGER ON NEXT PAGE

¹ All guarantees are based on the claims-paying ability of the issuer. Lump sum premium payments may cause a policy to become a Modified Endowment Contract, potentially creating additional tax consequences.

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751 Broad Street, Newark, NJ 07102-3777
IFS-A064676 Ed. 02/06 Exp. 08/07

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Basic Ledger Statement – Excerpt of Comparative Values

\$4,891,345 PruLife® SUL Protector, Type A (Fixed) Death Benefit - Cash Value Accumulation Test
 Male/Female – Both Age 67 - Preferred Best – Policy is a Modified Endowment Contract

Year	Age	Annual Premium Outlay	GUARANTEED Results Based On: Minimum Interest Rate of 3.00% & Maximum Charges		Non-guaranteed Results Based On: Illustrated Interest Rate 4.55% for 20 years, then 4.90%* thereafter and Current Charges	
			Cash Value	Death Benefit	Cash Value	Death Benefit
1	67	1000000	753455	4891345 <	826373	4891345 <
2	68	0	752840	4891345 <	847266	4891345 <
3	69	0	746717	4891345 <	868725	4891345 <
4	70	0	733717	4891345 <	890307	4891345 <
5	71	0	712044	4891345 <	911958	4891345 <
6	72	0	679316	4891345 <	933336	4891345 <
7	73	0	630529	4891345 <	951969	4891345 <
8	74	0	564008	4891345 <	969630	4891345 <
9	75	0	475471	4891345 <	985590	4891345 <
10	76	0	359967	4891345 <	999553	4891345 <
Sum		1000000				
11	77	0	211671	4891345 <	1026705	4891345 <
12	78	0	23420	4891345 <	1049691	4891345 <
13	79	0	0	4891345 <	1067732	4891345 <
14	80	0	0	4891345 <	1079916	4891345 <
15	81	0	0	4891345 <	1084831	4891345 <
16	82	0	0	4891345 <	1081132	4891345 <
17	83	0	0	4891345 <	1067349	4891345 <
18	84	0	0	4891345 <	1047914	4891345 <
19	85	0	0	4891345 <	1007563	4891345 <
20	86	0	0	4891345 <	952859	4891345 <
Sum		1000000				
21	87	0	0	4891345 <	885645	4891345 <
22	88	0	0	4891345 <	800248	4891345 <
23	89	0	0	4891345 <	691539	4891345 <
24	90	0	0	4891345 <	554680	4891345 <
25	91	0	0	4891345 <	382711	4891345 <
26	92	0	0	4891345 <	166092	4891345 <
27	93	0	0	4891345 <	0	4891345 <
28	94	0	0	4891345 <	0	4891345 <
29	95	0	0	4891345 <	0	4891345 <
30	96	0	0	4891345 <	0	4891345 <
Sum		1000000				

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< Indicates the **No-Lapse Guarantee** will be in effect for the entire policy year.

* This includes a non-guaranteed additional excess interest amount in years 21 and later. Current rate as of 1/1/2006, subject to change.

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