

Sales Strategy

Monthly publication describing timely and useful sales ideas and concepts.

THE POWER OF LIFETIME GIVING

(Give More by Giving Now)

INTRODUCTION

Many affluent clients express a desire to provide for their loved ones “after I’m gone.” Savvy estate planners have long known that one of the best ways to provide for loved ones is by planning now. Lifetime giving allows for privacy and probate avoidance, and may also increase the net amount passing to the heirs. This savings may be further leveraged through the use of life insurance to provide a substantial legacy to the client’s family.

TAX ADVANTAGES OF LIFETIME GIVING

Annual Exclusion Gifts. Annual exclusion gifts are a simple and easy way for clients to reduce their taxable estates. The annual exclusion gift¹ is the amount of money that may be annually gifted from any individual to any other individual without gift taxes and using unified credits. The maximum annual exclusion gift is \$12,000 per recipient per year and will be annually indexed for inflation in \$1,000 increments.

Taxable Gifts May Reduce Taxes. Advising a client to make a taxable gift may seem strange, but it may actually reduce the client’s total estate tax bill. How does this work? If a taxable gift is made at least three years before death, the gift taxes paid are usually not included in the client’s estate.² Therefore, the marginal estate tax bracket also may be reduced because the estate is reduced by the amount of the gift taxes paid.

EXAMPLE

Pat Grogan, a widower, has a total estate of \$7,000,000. He has already made gifts of \$1,000,000 (his gift-tax exemption amount) and also makes annual exclusion gifts to each of his two children. He knows his total estate tax liability may be nearly half of his estate if he does not begin making taxable gifts. He asks his financial advisor to illustrate the tax effect if he gives each of his children a gift of \$750,000.³ Assuming Pat Lives for another 10 years, here is what would happen.⁴

	<i>Without Gifting</i>	<i>With Gifting</i>
Beginning Estate	\$7,000,000	\$7,000,000
Total Gifts Made	\$0	\$1,500,000
Gift Taxes Paid	\$0	\$665,000
Remaining Estate	\$7,000,000	\$4,835,000
Estate Taxes at Death	\$3,695,000	\$2,649,250
After-Tax Estate	\$3,305,000	\$2,185,750
Gifts to Heirs	\$0	\$1,500,000
Net to Heirs	\$3,305,000	\$3,685,750
<i>Total Savings From Gifting Plan: \$380,750</i>		

Gifted Assets Appreciate Outside of Estate. Gifting allows transfer of rapidly appreciating assets out of an estate. These transfers enable the heirs to enjoy a larger ultimate gift because of the reduced estate taxes and also by removing the future appreciation from the estate.

EXAMPLE

Maria Donofrio, a widow, inherited \$10,00,000 when her husband died. \$1,000,000 of that total is stock in a closely held-company that is about to go public and is appreciating at 10% a year. Maria has already used her gift exclusion amount to make gifts to an Irrevocable Life Insurance Trust and purchase life insurance for her children. Maria believes that if she gives the stock to her children today, her total estate tax bill will be smaller than if she leaves them the stock at her death.⁵ Assuming Maria lives for 10 years after making the gift, the total savings from the gifting plan is \$1,391,245.⁶

	<i>Without Gifting</i>	<i>With Gifting</i>
Non-Stock Assets	\$9,000,000	\$9,000,000
Value of Stocks	\$1,000,000	\$1,000,000
Total Estate 2006	\$10,000,000	\$10,000,000
Gift of Stock	\$0	\$1,000,000
Gift Taxes Paid	\$0	\$435,000
Remaining Estate 2006	\$10,000,000	\$8,565,000
Non-Stock Estate Assets in 10 yrs.	\$9,000,000	\$9,000,000
Stock Estate Assets in 10 yrs.	\$2,593,742	\$0
Taxable Estate in 2016	\$11,593,742	\$9,000,000
Estate Taxes at Death	\$6,351,245	\$4,960,000
After-Tax Estate to Heirs	\$5,242,497	\$4,040,000
Gift to Heirs Stock Value 2016	\$0	\$2,593,742
Net to Heirs	\$5,242,497	\$6,633,742
Total Savings From Gifting Plan: \$1,391,245		

GIFTING AND LIFE INSURANCE

Gifting and life insurance are a particularly powerful combination. The annual exclusion allows \$12,000 to be gifted per person per year.⁷ If these gift dollars are used to purchase life insurance, the death benefit to the heirs often can be substantially leveraged as compared to the value of the original gift.⁸

CASE STUDY

Estate planners recommend gifting as a simple way of reducing their client's estate tax exposure. Some common methods of gifting are analyzed and compared in the case study.

Background. Sean and Kelley MacCauly are both 55 and have two children. Their estate is currently worth \$10,000,000, and has been growing at an after-tax rate of 3% a year. They have never done any planned gifting in the past, and are interested in the ways gifting can reduce their estate tax exposure.

Gifting to an Irrevocable Trust (IT) and Investing the Gifts.⁹ Many clients are reluctant to make gifts because they do not understand the benefits gifting provides, and they do not want to relinquish control of their property to their children. The MacCaulys are no exception. However, gifting to an IT and investing the money can provide more money for their heirs and keep control over the funds in an IT. In the following Gifting Analysis, the MacCaulys each gift the annual exclusion of \$12,000 annually to their children. This allows them to give away \$48,000 each year using

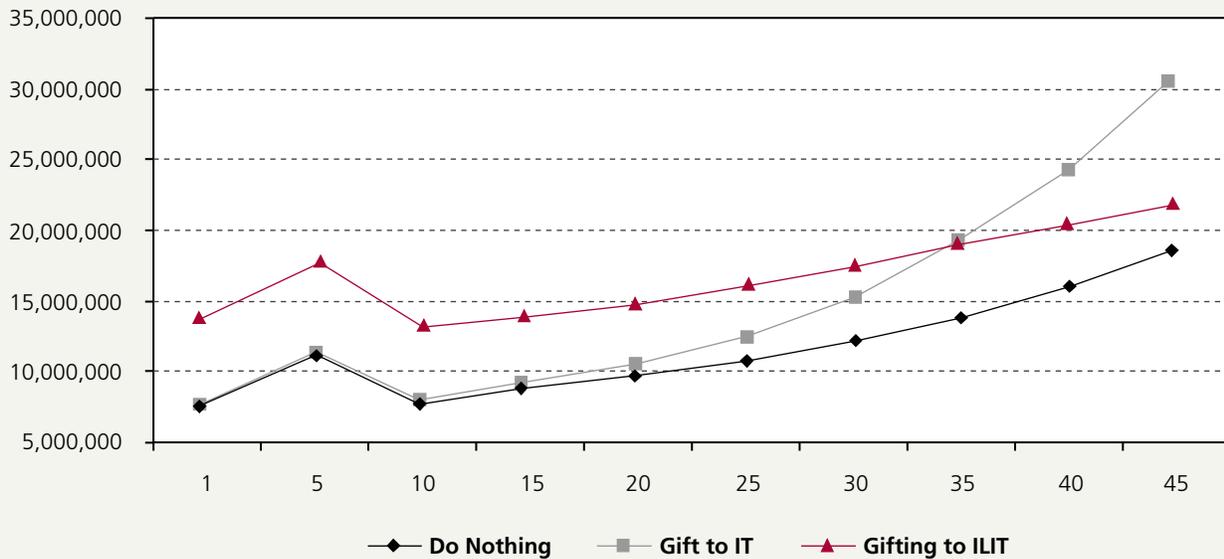
annual exclusion gifts. The MacCauleys will be able to pass \$8,959,684 through gifts and a bequest to their heirs through the 15th year, as compared to \$8,036,870 through the 15th year without gifting.

Gifts to an Irrevocable Life Insurance Trust (ILIT) and Purchasing Life Insurance.¹⁰ Although gifting in combination with an IT can provide substantial benefits, adding life insurance to the planning picture may be even more beneficial. If the MacCauleys use the \$48,000 annual gift to purchase a \$6,373,378 Survivorship UL-G¹¹ contract, the value to their heirs is greatly increased. In fact, with the insurance, a total of

\$14,042,436 is projected to be passed to their heirs in year 15 (assuming they both have died). This is \$6,005,566 more than if they made no gifts at all, and \$5,082,752 more than if they gifted money to an IT and invested it with an after-tax return of 7%. (See Chart below)

Advanced Markets has introduced the JH Solutions System to help demonstrate to your clients the benefits of life insurance as part of their lifetime gifting program. For more details, contact your Regional Director to obtain a sample of the module entitled "Gifting Analysis."

Comparison of No Gifting to an Irrevocable Trust & Investing and Gifting to an Irrevocable Life Insurance Trust



The data shown is taken from an illustration. It assumes a hypothetical rate of return and is not a representation of expected future results. Unless otherwise indicated, these values are not guaranteed.

NON-TAX ADVANTAGES OF LIFETIME GIVING

Lifetime giving provides more than just tax benefits. Lifetime giving allows clients to:

- see loved ones enjoying the gifts now;
- protect gifted assets from the donor's creditors
- avoid probate for gifted assets and protect family privacy; and
- use gifts to purchase life insurance, which may increase the amount of money left to the heirs.

SUMMARY

Lifetime giving is a powerful and simple tool in the estate planning arsenal. Gifting can reduce estate taxes, maximize gifts to loved ones, and safeguard the family's privacy. However, the real power of lifetime giving becomes apparent when it is combined with purchasing life insurance in an ILIT.¹¹ Life insurance often multiplies the value of the gift and provides a lasting legacy to future generations.

1 The annual exclusion amount is \$11,000 in 2005.

2 Under IRC Sec. 2035, gift taxes paid and certain gifts made within three years of death will be includible in the decedent's estate when calculating the gross estate. The three-year rule applies to certain gifts such as life insurance proceeds, and gifts with a retained life estate.

3 For purposes of simplicity, we are assuming the following: 1) the current year is 2006, 2) he has no annual exclusions available, and 3) the value of the rest of the estate remains the same (no appreciation/reduction).

4 See Footnote 2

5 For purposes of simplicity, we are assuming the following: 1) the current year is 2006, 2) she has no annual exclusions available, and 3) the other assets in the estate experience no appreciation or depreciation.

6 See Footnote 2

7 See Footnote 1

8 See Footnote 2

9 Trusts should be drafted by an attorney familiar with such matters in order to take into account income and estate tax laws (including generation-skipping tax). Failure to do so could result in adverse tax treatments of trust proceeds.

10 The premiums paid for Mr. & Mrs. MacCauly's new Survivorship UL-G contract are based on rates in Florida for a male, age 55, preferred non-smoker and female Florida resident, age 55, preferred non-smoker. Survivorship UL-G's death benefit is guaranteed for 45 years at this premium. However, at the current crediting rate of 5.25% and current policy charges, neither of which is guaranteed, the policy could be kept in force until death with an annual premium of \$48,000.

11 Assuming the proposed initial gift was not a fraudulent conveyance meant to inhibit creditors.

John Hancock insurance products issued by: John Hancock Life Insurance Company, Boston, MA 02117.

Sales Strategy is produced by John Hancock's Advanced Markets Group. We can be reached at 1-888-266-7498, option 3.

This material is for informational purposes only. Although many of the topics presented may also involve tax, legal accounting or other issues, neither John Hancock nor any of its agents, employees, or registered representatives are in the business of offering such advice. The above material was not intended or written to be used, and it cannot be used, for the purpose of avoiding any penalty that may be imposed by the Internal Revenue Service. The above material may have been written to support the promotion or marketing of the transactions or topics addressed by the written material. Individuals interested in these topics should consult with their own professional advisors to examine legal, tax, accounting or financial planning aspects of these topics. MLI1216045031 Expires 12/31/06



John Hancock Life Insurance Company (U.S.A.)
197 Clarendon Street, Boston, MA 02116.

©2005. John Hancock Life Insurance Company (U.S.A.). All rights reserved.