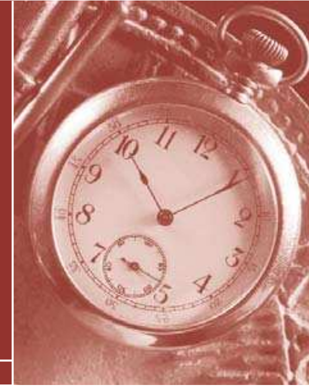
John Hancock
LIFE INSURANCE



Sales Strategy
The Dynasty Trust

LEVERAGING THE GSTT EXEMPTION TO CREATE A LASTING LEGACY

INTRODUCTION

With baby boomers anticipating large inheritances, and more states allowing trusts to last for an unlimited duration,[1] clients need to use their exemption from the generation-skipping transfer tax (GSTT) effectively. Purchasing life insurance inside of a Dynasty Trust can enable clients to transfer millions of dollars to future generations while shielding trust assets from gift, estate, and generation-skipping transfer taxes. The increase in the GSTT exemption in the next few years offers a great opportunity for multi-generational Dynasty Trust planning.

WHAT IS THE GENERATION-SKIPPING TRANSFER TAX (GSTT)?

The federal gift and estate tax system is designed to tax accumulations of wealth when they are transferred to each succeeding generation. Without the generation-skipping transfer tax (GSTT), a wealthy individual could potentially circumvent the estate and gift tax system by making gifts directly to grandchildren or future generations, avoiding the estate tax which would otherwise occur in one or more "skipped" generations. Alternatively, the individual could avoid estate tax by placing assets in trust for the benefit of children, grandchildren, and future generations.

In 1986, Congress enacted the current GSTT system. In simple terms, the GSTT is a flat tax (at the highest current estate tax rate) imposed on transfers that "skip" at least one generation, and it is imposed in addition to any estate or gift tax due on the transfer. For example, a gift from a grandparent to a grandchild is a generation-skipping transfer that may be subject to the GSTT.[2] A gift from a grandparent to a trust that has one or more grandchildren as beneficiaries, and may otherwise be subject to the GSTT, can avoid the GSTT if the grandparent allocates sufficient GSTT exemption to the trust.[3]

WHAT IS THE GSTT EXEMPTION?

Each individual has an exemption from the GSTT, which may be used during lifetime or at death. From 2006 through 2008, this exemption will be $2,000,000 per person, and in 2009 the exemption amount will increase to $3,500,000 per person.[4] The key to effective use of the GSTT exemption is to allocate the available exemption to assets that offer maximum leveraging of the exemption, such as life insurance.

WHAT IS A DYNASTY TRUST?

A Dynasty Trust is a popular name for a special type of Irrevocable Life Insurance Trust (ILIT).[5] Unlike a traditional ILIT, the Dynasty Trust is designed to continue for several generations. The Dynasty Trust can give each generation access to the trust assets (such as for health, education, maintenance, and support), while keeping the remaining trust assets outside of the beneficiaries' taxable estates for as long as state law permits. In addition to saving estate taxes in future generations, a Dynasty Trust can protect trust assets from creditors of the trust's beneficiaries (including a divorcing spouse), and can facilitate wise management of the family's wealth.

HOW IS A DYNASTY TRUST SET UP?

One or more grantors will create a Dynasty Trust and make lifetime gifts to the trust.[6] The grantor(s) will allocate GSTT exemption to all of the lifetime gifts to the trust on federal gift tax returns. The trustee of the Dynasty Trust purchases life insurance, often a survivorship policy, which pays a death benefit to the trust after both grantors are deceased.
If the GSTT exemption allocated to the trust is sufficient to cover all of the lifetime gifts made to the Dynasty Trust, the entire death benefit received by the trust, and any other assets held in the trust, should be exempt from GSTT!
The following example illustrates how a married couple can create, fund, and allocate their GSTT exemptions to a Dynasty Trust.

CASE STUDY: JOHN AND ALISON SMITH

John Smith (age 67) and his wife Alison (age 62) have two children and three grandchildren, and a combined estate of $10,000,000. John and Alison each currently make $12,000 annual exclusion gifts to their children and grandchildren, but neither of them has used their GSTT exemptions.[7] Together, they can gift $120,000 annually, with just their annual exclusions.[8] John and Alison know that their lifetime gift exemptions will also allow each of them to transfer $1,000,000 during their lifetimes without paying any federal gift tax. They do not have any life insurance and have decided that they will need to purchase a $5,000,000 survivorship life insurance policy inside a Dynasty Trust to cover their expected liquidity needs at death.

Life Insurance with Guarantees. The trustee of the Dynasty Trust decides to purchase John Hancock's new Protection Survivorship UL-G (Protection SUL-G) product on the lives of John and Alison.[9] At their ages, the trustee can purchase a $5,000,000 survivorship policy with an annual premium of $99,383.40 for 15 years.[10]

Benefits for Heirs. After John and Alison are deceased, the trustee can use the trust income and principal for the benefit of their children, grandchildren, and later descendants. Because John and Alison will allocate GSTT exemption to the gifts to the trust, the entire death benefit will be fully exempt from GSTT, and the Dynasty Trust should not be subject to estate tax for several generations after John and Alison are deceased, as long as the assets remain in the trust.[11]

Assumptions. The table below illustrates the potential benefits of Dynasty Trust planning for John and Alison and their descendants. These calculations assume that the assets remain in trust and no distributions are made to the beneficiaries (the amount shown below is what would be available to each generation). The property available to heirs shows the total estate assets, including the Dynasty Trust assets, less the estimated estate taxes that will be due in year 25 (John and Alison's joint life expectancy).
All trust assets (other than the life insurance policy), as well as the assets included in John and Alison's estate, are assumed to grow at a net after tax rate of 4%.[12] The table below compares three different possible scenarios: no lifetime gifting, lifetime gifts to a Dynasty Trust with a growth rate of 4%, and lifetime gifting to a Dynasty Trust which owns a $5,000,000 survivorship life insurance policy.

As the chart below indicates, by making gifts to a Dynasty Trust with insurance and properly allocating their GSTT exemptions, John and Alison can significantly increase the net to their heirs for several generations to come.

Property Available to Heirs (Net of Estate Tax)	Scenario 1 No Gifting	Scenario 2 Lifetime Gifts to a Dynasty Trust/No Insurance	Scenario 3 Lifetime Gifts to a Dynasty Trust with Insurance
Year 25 (Parents Life Expectancy) For Children	$13,015,213	$14,700,156	**$16,636,624**
Year 41 (Children's Life Expectancy) For Grandchildren	$10,969,763	$15,545,769	**$19,172,736**
Year 65 (Grandchildren's Life Expectancy) For Great-Grandchildren	$12,653,477	$26,021,285	**$35,318,306**

The data shown is taken from an illustration. It assumes a hypothetical interest crediting rate and may not be used to project or predict investment results.

In addition to increasing the amount of property available to their heirs, John and Alison can also reduce their estimated estate tax liability by funding a Dynasty Trust with lifetime gifts. In the first scenario, with no gifting, the expected estate tax liability on their total estate in year 25 is $12,653,477, but in Scenarios 2 and 3, after making gifts to fund the Dynasty Trust, the expected estate tax liability in year 25 is $11,907,595.

GUARANTEES TAKE THE GUESSWORK OUT OF DYNASTY TRUST PLANNING

When using life insurance to leverage the GSTT exemption, it is important to make sure that required premium payments do not exceed the exemption available. John Hancock's Protection SUL-G offers a Policy Protection Rider to age 121 of the younger life insured. As long as the Policy Protection Rider premiums, as illustrated, are paid in a timely manner, the death benefit will stay in force, even if the net cash surrender value falls to zero. Clients have the flexibility to select the Policy Protection Rider guarantee duration most appropriate for their risk tolerance, from as little as 15 years to as long as their lifetime. Protection Survivorship UL-G offers clients competitive premiums, and a combination of the flexibility, strength, and security that they need to provide for their heirs.

SUMMARY

The Dynasty Trust can dramatically increase the value of the inheritance that your client's heirs will ultimately receive by reducing estate taxes in future generations. Life insurance inside of a Dynasty Trust can help your clients use the GSTT exemption effectively. John Hancock's universal life insurance products are ideal for Dynasty Trust planning because they allow your clients to select the death benefit guarantees that are most appropriate for their planning needs, while preserving the flexibility that makes universal life insurance so attractive.

The Advanced Markets Group has created the JH Solutions System to help demonstrate to your clients the benefits of using life insurance as part of a comprehensive estate plan, such as with a Dynasty Trust.

For more information on Dynasty Trusts or JH Solutions, contact your John Hancock representative or the Advanced Markets Group at 1-888-266-7498, option 3.

1. At least twenty-two states have abolished the Rule against Perpetuities, and in those states trusts can either have unlimited duration or last for a longer term of years. These states currently include Alaska, Arizona, Colorado, Delaware, Idaho, Illinois, Maine, Maryland, Missouri, Nebraska, New Hampshire, New Jersey, Ohio, Rhode Island, South Dakota, Virginia, District of Columbia, Wisconsin, Wyoming (trusts can last for 1000 years), Utah (1000 years), Florida (360 years), and Washington (150 years).
2. To the extent that this lifetime gift directly to a grandchild qualifies for the annual gift tax exclusion under Internal Revenue Code (IRC) section 2503(b), the GSTT will not apply. IRC section 2642(c).
3. The gift may also avoid the GSTT if (1) the gift qualifies for the predeceased ancestor exception in IRC section 2651(e) or (2) the transfer meets the IRC section 2642(c) exception. Section 2642(c) provides that certain “direct skips” to a trust created for the benefit of a single beneficiary will not be subject to GSTT if the trust estate will be included in the beneficiary’s gross estate at death, and the transfer qualifies for the annual gift tax exclusion or the qualified tuition or medical expense exclusion under IRC Section 2503.
4. The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) has increased the estate and GST tax exemptions to $2,000,000 per person in 2006-2008 and $3,500,000 in 2009. However, the provisions of EGTRRA expire after December 31, 2010. The estate and GST tax will be repealed for one year in 2010, but unless the law is changed before December 31, 2010, the estate tax exemption will be $1,000,000 per person and the GSTT exemption will be $1,060,00 in 2011. This Sales Strategy assumes that EGTRRA will not be extended after 2010.
5. Trusts should be drafted by an attorney familiar with such matters in order to take into account income and estate tax laws (including the generation-skipping transfer tax). Failure to do so could result in adverse tax treatment of trust proceeds.
6. The grantor(s) often use any GSTT exemption still available at death by including a provision in a revocable trust or will to transfer such amount to the Dynasty Trust. Coordinating the grantor(s) estate plan(s) with lifetime gifts can be critical to properly funding the Dynasty Trust.
7. This example assumes that their annual exclusion gifts to the grandchildren also qualify under IRC section 2642(c), so these gifts do not use any of their GSTT exemptions.
8. John and Alison are both grantors of the Dynasty Trust, so each one can gift $60,000 per year using their current annual exclusions. However, in order to qualify for the annual exclusion, the gifts to the trust must be “present interest gifts” and trust beneficiaries must have “Crummey” rights of withdrawal over the gifts.
9. This example assumes that John and Alison are both superpreferred, nonsmokers and are Florida residents. Products and features may not be available in all states. Guaranteed product features are dependent upon minimum premium requirements and the claims-paying ability of the issuer.
10. The example assumes that John and Alison will gift exactly the premium amount to the trust each year, using their annual exclusions. Their joint life expectancy is twenty-five years.
11. Clients making annual exclusion gifts to a Dynasty Trust should generally allocate GSTT exemption to these gifts unless the gifts qualify under IRC Section 2642(c) (see endnote 3). When annual exclusion gifts are made to a Dynasty Trust, some estate planners suggest limiting these gifts to the greater of $5,000 or 5% of the trust estate per beneficiary. See IRC Section 2514(e).
12. This example assumes a current crediting rate of 5.25% on the life insurance policy.

John Hancock®

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

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