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Spousal Lifetime Access Trust (SLAT)

The predictability of whole life insurance for a trustee

Wealthy married couples often create Irrevocable Life Insurance Trusts (ILITs) to own life insurance on their lives. If properly drafted, the trust will receive the life insurance proceeds at the insured's death, free of income and estate taxes.

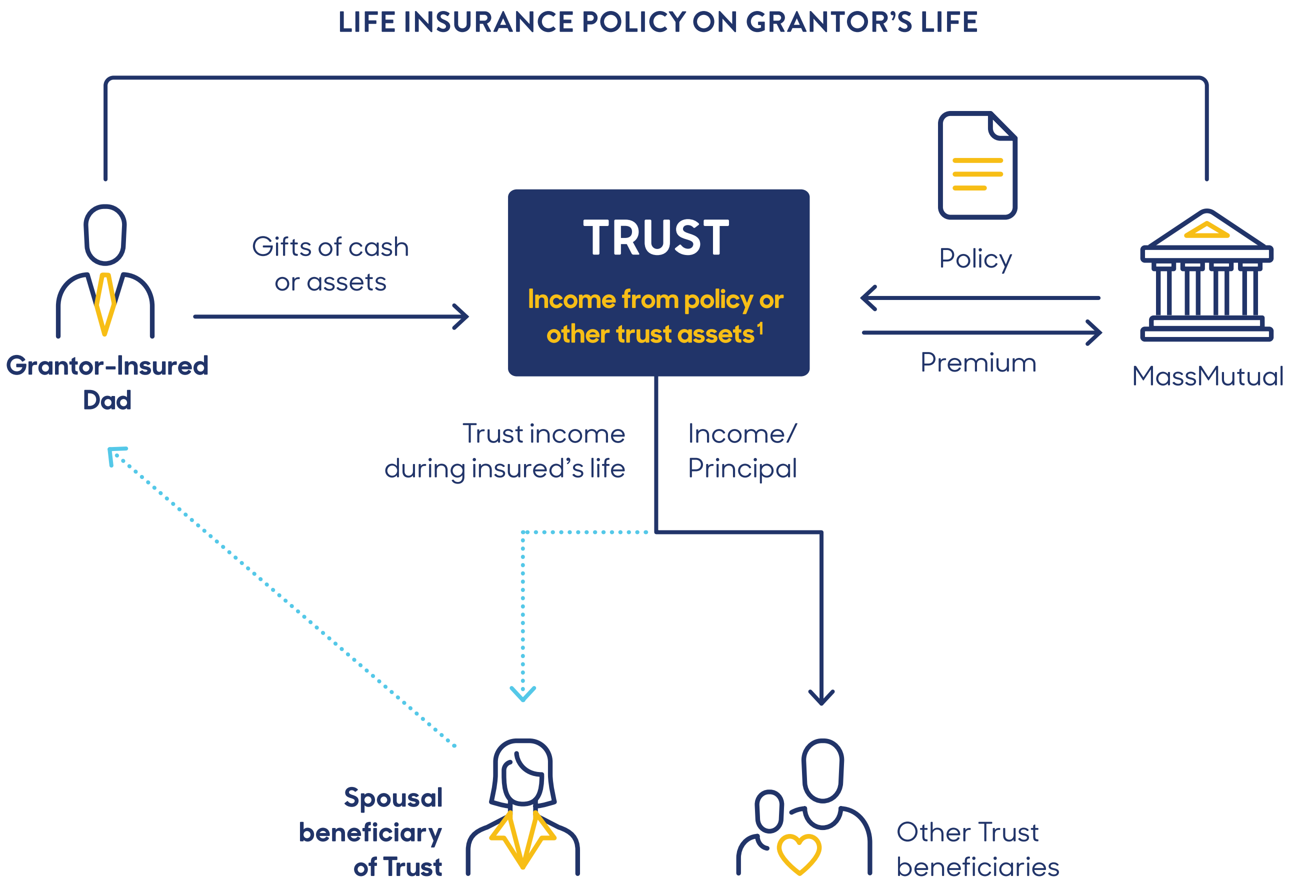
Concern.

A common complaint about ILITs is that the grantor-insured (the person who creates the trust — "trust grantor"— and who is the insured on the life insurance policy owned by the trust) loses control over the assets transferred to the trust, including access to the life insurance policy's cash value during the insured's lifetime.

Solution.

By including spousal access provisions in the ILIT, which allows one of the spouses to be a beneficiary of the trust while the other spouse is the trust grantor, the trustee can make distributions from the policy's cash values during the insured's lifetime to benefit a spouse. In this way, the grantor spouse has indirect access to policy values through the non-grantor spouse.

How a Spousal Access Trust Works:



[1] Distributions under the policy (including cash dividends and partial/full surrenders) are not subject to taxation up to the amount paid (cost basis). If the policy is a Modified Endowment Contract, policy loans and/or distributions are taxable to the extent of gain and are subject to a 10% tax penalty. Access to cash values through borrowing or partial surrenders will reduce the policy's cash value and death benefit, increase the chance the policy will lapse, and may result in a tax liability if the policy terminates before the death of the insured.

There are three ways to fund a Spousal Lifetime Access Trust with life insurance:

1 Using a survivorship policy

2 Using a single life policy

3 Using 2 spousal lifetime access trusts

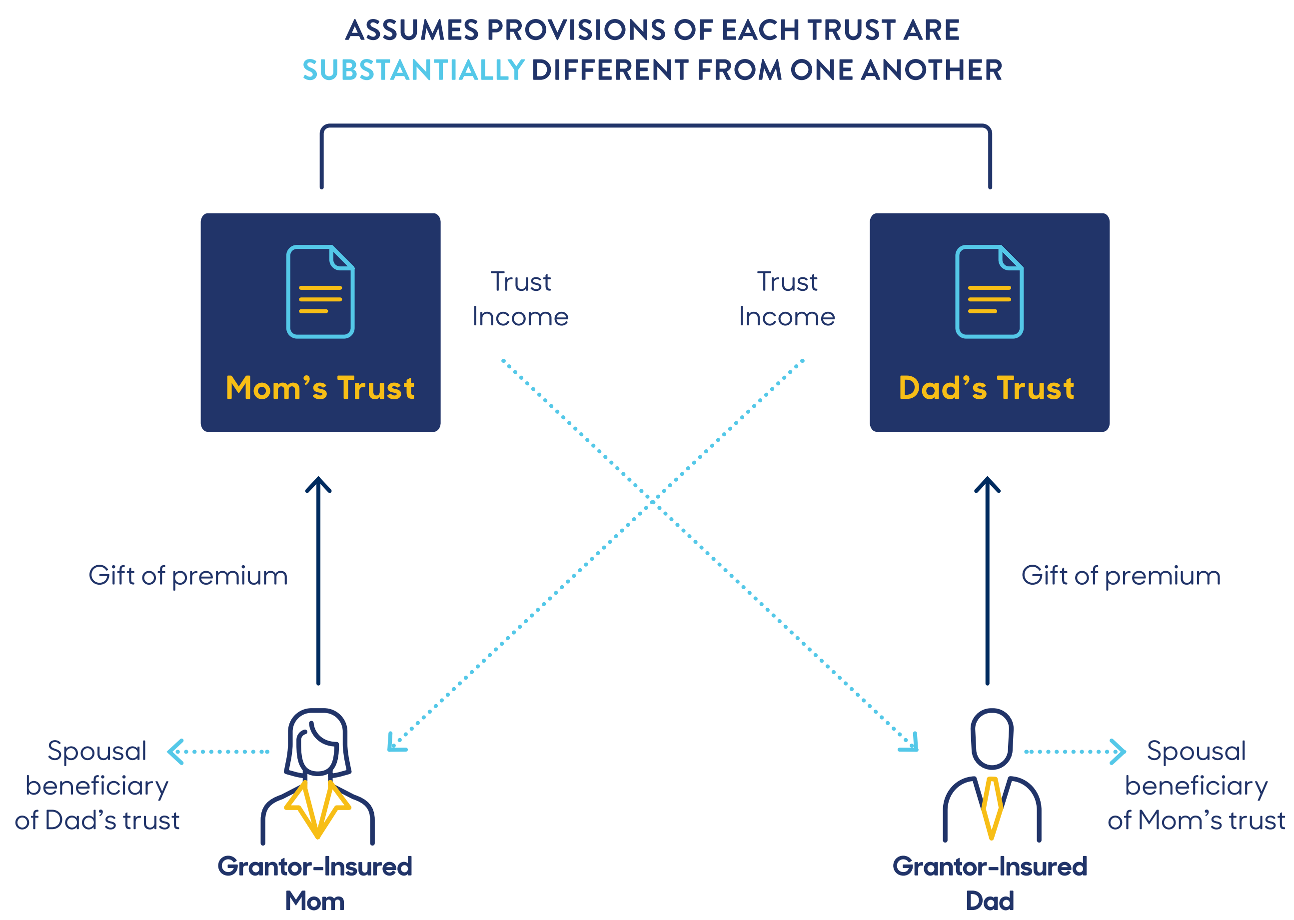
SURVIVORSHIP POLICY	SINGLE LIFE POLICY	TWO TRUSTS OWN A SINGLE LIFE POLICY EACH
• Neither spouse is named trustee. • Adult children can be named as trustee, or an independent trustee can be chosen. • One of the two in the couple is the grantor of the trust (establishes trust and makes gifts to trust). • Insurance covers both lives. • The non-grantor spouse is spousal beneficiary who may receive income from trust assets, including from the policy's cash values. • The non-grantor spouse may not make direct or indirect contributions to the trust.[2] • **CONSIDER:** With a survivorship policy, consider how future premiums will be paid at the death of the first spouse.	• Insurance is on the grantor-spouse. • The adult children, or the non-insured spousal beneficiary, can be named as trustee. However, distributions made to the spousal beneficiary is limited to the spouse's need for health, education, maintenance and support. • The insured spouse is only one to make contributions to trust, and only from property that is separate from the spouse's.[3] • The uninsured spouse is trust beneficiary who may receive income from the trust, including in the form of policy surrenders or loans.[1]	• Each spouse creates (is a grantor of) a trust, and is the insured on a single life policy owned by the respective trust. • Each non-grantor spouse is spousal beneficiary of the other's trust. • Naming an independent trustee for each trust is best. • The non-grantor spousal beneficiary may receive distributions from the trust for support and maintenance, at the discretion of an independent trustee. • **CONSIDER:** Beware of the reciprocal trust issue.[4]

[2] Caution is required in the funding of a spousal access trust. If the grantor funds the trust by writing a check out of a joint account or out of community property in a community property state, the Internal Revenue Service (IRS) will view the transaction as a gift being made by each spouse in the amount of one-half each. This would create a problem since the beneficiary-spouse is treated as making a gift to a trust in which he or she is a beneficiary. Under IRC §2036, one-half of the value of that trust will be includable in the spouse's taxable estate. To avoid giving the beneficiary spouse any incidents of ownership with a survivorship spousal access trust, the authority to make distributions to the surviving spouse may need to be limited to an independent trustee with absolute discretion. See PLR 200617008. PLRs are merely an IRS interpretation of law and are binding only upon the taxpayers to whom they are issued.

[3] Spouses can split gifts for annual gift tax exclusion purposes and will be required to file a gift tax return. In 2022, individuals can make an annual gift of up to $16,000 to any number of people, free of gift tax. This type of gift is referred to as an annual exclusion gift. The tax-free annual exclusion gift can also be made directly to a trust, to benefit each of the beneficiaries of a trust, provided that each is notified of the gift and given the right to withdraw it within a specified period of time.

[4] The reciprocal trust doctrine refers to the situation when similar trusts are created between spouses to avoid estate tax under the literal terms of the internal revenue code but there is no change in the economic position of each donor with respect to the property. Under the doctrine, the trusts are not substantially different from one another in substance. Therefore, assets will be included in the estate of the grantor. Trusts should be drafted by attorneys familiar with such matters.

What two Spousal Lifetime Access Trusts may look like:



To address the reciprocal trust doctrine, the attorney drafting the trusts can include materially different provisions in each trust to make them sufficiently different in substance from one another. Trusts should be drafted by attorneys familiar with such matters in order to take into account income and estate tax laws (including generation-skipping transfer tax.) Failure to do so could result in adverse tax treatment of trust proceeds.

Life Insurance

Consider the flexibility of MassMutual's Whole Life 12 Pay for a Spousal Lifetime Access Trust using a single life policy. In the example below, Jonathan, age 48 today, creates a SLAT and makes gifts of annual premiums to the trust so it can fund the policy on his life. The below figures illustrate both the net death benefit at given ages, as well as net cash values available to the trustee to make potential distributions to Jonathan's spouse, who is a beneficiary of the trust:

MassMutual Whole Life 12 Pay with a $2M Initial Death Benefit on a Male, Age 48
Ultra-Preferred Non-Tobacco Risk. Annual Premium for 12 Years: $103,840
Cumulative Premiums Paid: $1,246,080

	AGE 75	AGE 85	AGE 90
Net Cash Value End Year	$2,922,713	$4,614,025	$5,646,010
IRR on Net Cash Value End Year[5]	4.00%	4.21%	4.20%
Net Death Benefit End Year	$4,057,296	$5,463,682	$6,328,898

This is a supplemental illustration and is not valid unless accompanied by or preceded by a Whole Life 12 Pay basic illustration. Refer to the Basic Illustration for guaranteed elements and other important information. Click here for the Basic Illustration: **Illustration**

These illustrated amounts are not guaranteed. They include dividends, which are neither estimates nor guarantees, that have been applied to purchase paid-up additions based on the 2022 dividend schedule. The dividend schedule is reviewed annually, and it is likely that dividends in future years will be lower or higher depending on the Company's actual experience. For this reason, we strongly recommend that you look at a lower dividend schedule illustration. Refer to the Basic Illustrations for guaranteed elements, assumptions, explanations and other important information.

[5] The IRR refers to the internal rates of return which are a measure that can be used to evaluate performance and is based on the current dividend schedule. They are an amount at which outlays (out-of-pocket costs) up to that year must be compounded each year to generate the net cash value, in this example.

Benefits

- The trust receives the death benefit free of income and estate tax.
- An ILIT may protect assets from creditors[6].
- Life insurance can increase the amount left to heirs.
- The SLAT allows distributions to be made to the grantor's spouse and children during his/her lifetime, allowing access to the policy cash value.
- The trustee can make distributions to provide the grantor's spouse with supplemental retirement income or financial support. If the trustee is an independent trustee, the discretion to make distributions is broad. If the trustee is the spouse in a SLAT funded with a single life policy on the life of the grantor, then the distributions will be limited to the health, education, maintenance and support (HEMS) needs of the spousal beneficiary.

Considerations

- Gifts and transfers to an ILIT are irrevocable and may only be used for the benefit of trust beneficiaries.
- Distributions under the whole life policy (including cash dividends and partial/full surrenders) are not subject to taxation up to the amount paid into the policy (cost basis). If the policy is a Modified Endowment Contract, policy loans and/or distributions are taxable to the extent of gain and are subject to a 10% tax penalty if the policyowner is under age 59½.
- Access to cash values through borrowing or partial surrenders will reduce the policy's cash value and death benefit, increase the chance the policy will lapse, and may result in a tax liability if the policy terminates before the death of the insured.

Contact your Managing Director, or Advanced Sales at 1-800-601-9983 Option #2 or email MMSDAdvancedSales@MassMutual.com

[6] Protections afforded life insurance products are a matter of state law.

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