

# Planning for Estate Taxes in an Uncertain World

*How permanent cash life insurance can have far-reaching applications*

BY MIKE MULLARNEY

**F**rom an estate planning perspective, this has been quite a year.

Many years ago, during President George W. Bush's term, I sat in an estate planning presentation in which the main stage speaker asked for a show of hands of how many people thought the estate tax would be repealed. Of the 1,000 or so professionals in the room, all of them experts on estate planning, not one hand went up.

Well, here we are, over halfway through 2010, and there's no federal estate tax. Come Jan. 1, 2011, unless legislators take action, the value of an estate above \$1 million will be subject to estate tax at rates up to 55 percent.

In addition to the uncertainty surrounding the estate tax, there is pressure on Congress to limit the ability to pass wealth to successive generations without taxation. This has come in the form of proposed legislation requiring a 10-year minimum term for grantor-retained annuity trusts (GRATs) and limitations on the use of valuation discounts.

The uncertainty of the estate tax and possible limits on planning alternatives add additional uncertainty to estate planning. But uncertainty is nothing new to estate planners; it's part of what we do. All estate plans must take into account the fact that we don't know when our clients will die, how much their estates will be worth, or even their family situation at their death. Legislative uncertainty just adds one more item to the list.

In the face of all this uncertainty, it's tempting for clients (and advisors, too) to throw up their hands and give up. But to do no planning is never a prudent strategy. Clients have people they want to provide for. In order for the clients to make sure their estate planning objectives are met, they must have a well thought-out plan in place. In this environment, an estate plan continues to be a necessity, but, now more than ever, that plan must include flexibility.

And that's where permanent cash value life insurance fits in.

A life insurance death benefit can be an important tool for

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solving a variety of estate planning challenges; the policy's cash value adds the ability to adapt to future changes. The following examples illustrate planning with life insurance and the flexibility it brings.

## 1 Providing for his children

John owns an engineering firm that he'd like to leave to his son Jack, who is currently working in the business. John has two other children, Steve and Kay, who are not involved in the business. John wants to pass his business to Jack, but doesn't want to disinherit the other two.

Like most business owners, the business comprises nearly all of John's estate, leaving him few assets he can pass on to Steve and Kay. John decides to buy a policy for himself; its death benefit will provide additional value that John can leave to Steve and Kay.

Since John's estate is probably not large enough to generate estate tax at his death, he chooses to own the policy himself. This allows him to use the policy cash value if circumstances change. For example, if he needs additional retirement income, he can access the cash value on a tax-favored basis for his income needs.

## 2 Supporting special needs children

Kate and Jamie have a child with special needs — Rosie. They are confident that they can provide for Rosie's needs as long as they are alive, but want to make sure there are enough financial resources to provide for Rosie after their deaths. Kate and Jamie purchase a life insurance policy naming their daughter as a beneficiary.

Because they have significant assets, they decide to purchase the policy in an irrevocable trust so that the death benefit is not subject to estate tax. The trust is specially designed so that it doesn't jeopardize Rosie's eligibility for government benefits. If circumstances change such that Kate and Jamie need additional resources for Rosie, and if the trust is drafted flexibly, the trustee can access policy values to provide for Rosie's care while Kate and Jamie are still alive.

## 3 A loan to a child

A successful real estate developer, Walter has an estate that has grown to \$20 million. He'd like to pass the estate on to his two children. Although he has a significant estate, it is mostly illiquid. He understands that he'll face a significant estate tax at his death, and doesn't want his assets to be liquidated to pay the tax. He purchases a life insurance policy owned by an irrevocable trust so that the death benefit doesn't add to his estate tax bill.

Walter's daughter, a chef, would like to open her own restaurant, but needs \$1 million of capital to do so. Walter is willing to help her, but doesn't have the liquidity in his assets. Assuming the trust allows for it, the trustee can access the cash value in the policy and make a loan or distribution to the daughter. Alternatively, the trustee could pledge the policy as security for a loan from a bank to fund the daughter's restaurant.

Clients need planning in order to achieve their estate planning objectives — but the plan needs to be flexible in order to deal with changing circumstances. Permanent cash value life insurance can help clients solve their estate planning needs while also providing flexibility. “

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