SPOUSAL LIFETIME ACCESS TRUST (SLAT)

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A Spousal Lifetime Access Trust (SLAT) is an irrevocable trust created by one spouse for the benefit of the other spouse, usually funded with a life insurance policy on the life of the donor spouse. While on the surface the SLAT might seem like any other irrevocable life insurance trust (ILIT), it has one key difference from the ILIT — the ability to make distributions to the beneficiary spouse during the grantor spouse's lifetime. In its simplest form, the donor spouse makes cash gifts to the trust equal to the premium payments required to fund an insurance policy. Alternatively, the donor spouse can gift income-producing assets, which will shelter those assets from the reach of creditors and which moves the assets out of the donor's taxable estate while still ensuring that the assets are available for the couple's use through the beneficiary spouse's interest in the SLAT.

SLAT TAX BENEFITS

Like all irrevocable trusts, there are many options available for funding the SLAT, including annual exclusion gifts, lifetime exemption gifts, private loans and third-party loans from a commercial lender. The SLAT can be drafted as a defective grantor trust, which leaves the grantor still paying the income taxes on the trust's assets, or as a dynasty trust, which utilizes the donor's generation-skipping transfer (GST) tax exemption. It is important to also note that, when funded with life insurance, the SLAT will be able to take advantage of the three federal income tax advantages of life insurance:

- Tax-deferred growth of cash value
- Tax-free withdrawals of cash value
- Tax-free death benefit

ASSET PROTECTION PLANNING

If the trust is properly structured, the assets should be protected from the donor spouse's creditors. In addition, the trust structure may provide asset protection for the beneficiary spouse and family member beneficiaries. Rather than making distributions from the SLAT directly to a beneficiary, the SLAT trustee can withhold distributions or make distributions for the benefit of a beneficiary, such as by paying bills directly.

SURVIVORSHIP INSURANCE PLANNING

A SLAT can also be funded with a survivorship policy, which insures the lives of both spouses. Survivorship insurance, when utilized, is intended to provide estate tax liquidity at the second death. However, if the couple desires flexibility in their estate tax planning, the policy can be funded to have significant cash value that can be accessed by the beneficiary spouse during his or her lifetime. In addition, the death benefit can be reduced, freeing up policy cash value, which can be returned to the couple through distributions to the beneficiary spouse. If the couple no longer wants the coverage, the SLAT trustee can surrender the policy and distribute the policy surrender proceeds to the couple through a distribution to the beneficiary spouse. The beneficiary spouse should not be a trustee of a survivorship SLAT in order to avoid having the policy death benefit included in the beneficiary spouse's estate if he or she is the survivor. Often, a single life policy on the life of the donor spouse is purchased to provide a source of funds to pay any remaining premiums on the survivorship policy, to pay off any loans from the donor spouse and to provide for the beneficiary spouse's needs upon the death of the donor spouse.

SLAT FUNDED WITH A SINGLE LIFE INSURANCE POLICY

Husband sets up the SLAT and funds it with an initial cash gift. The trustee of the SLAT uses the initial gift to purchase an insurance policy on husband's life. Wife is named as the beneficiary of the trust to receive income and principal for her lifetime. Each year, husband makes additional cash gifts to pay the annual premium on the policy.

Upon husband's death, the SLAT trustee receives the death benefit income and estate tax free. The trustee invests the SLAT assets for the primary benefit of wife. During wife's lifetime, the trustee pays wife income and principal to maintain her lifestyle. Upon her death, the SLAT can terminate in favor of the couple's children, or it can continue for the benefit of the children and grandchildren.

If the insurance policy is funded to generate cash value, the couple can access the cash value through principal distributions to the beneficiary spouse. The SLAT trustee can take income-tax-free withdrawals from the policy to make distributions to wife. These distributions can be used by the couple for supplemental retirement income, to pay education expenses or to cover medical costs.

BENEFITS OF A SLAT

- One spouse provides income or wealth replacement for the other.
- Policy cash values remain available to the couple during the insured spouse's lifetime.
- Any assets gifted to the SLAT pass free of estate taxes in both spouses' estates.
- The policy death benefit is received by the SLAT free of income and estate taxes.
- The beneficiary spouse can be the sole trustee of the SLAT during his or her lifetime.
- The SLAT may provide asset protection for the beneficiary spouse and other family member beneficiaries.
- The policy death benefit can be used to provide estate tax liquidity in the insured's estate.
- The SLAT can be structured to be a dynasty trust, with all trust assets exempt from the federal GST tax.
- The SLAT can be structured as an intentionally defective grantor trust for federal income tax purposes, which may further leverage the tax efficiency of the SLAT.

CONSIDERATIONS

- Provisions of the federal gift tax must be carefully considered.
- In community property states, separate property must be used to fund the SLAT.
- If each spouse will create a SLAT for the other, the "reciprocal trust doctrine" must be considered.
- If a survivorship SLAT will be created, consideration must be given to who will serve as the independent trustee.

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