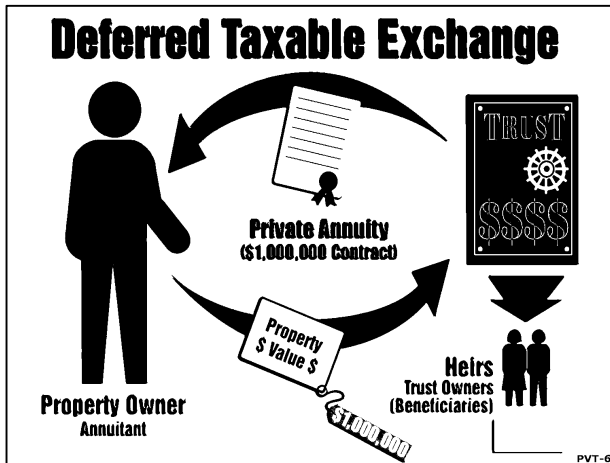


Script for Presentation of

Premier VI Private Annuity/Trust, Capital Gains Deferral

Note to Presenter: A good handout or study guide to go with this presentation is NAFEP's, 7 page *Deferring Capital Gains Taxes...* booklet. Instead of or in addition to that handout, you may print the graphics from Power Point, 3 to a page, with several horizontal lines drawn to the right (see example below). Giving this as a handout allows easy note taking by the clients. To do this, open the NAFEP Power Point file entitled, *Private Annuity Show*. Next select "File" from the toolbar, then "Print." This opens the printer dialog box. In the printer dialog box, under the "Print Range" selection, choose "All." Under the "Print What" selection choose "Handouts." Under the "Handouts," "Slides Per Page" selection choose "3." At the bottom of the dialog box, check "Pure Black and White" and "Frame Slides." Click the "OK" button to start the print job.



Example of 1/3 Page of Power Point Print Out

Note 2 to Presenter: The presentation is much more interesting and greatly increases the listeners' understanding if you allow questions throughout. If someone asks a question which will be directly covered in a later graphic, it is best to tell the questioner that you will cover that question later on. Without questions this presentation takes about 25 minutes, and about 40 or 45 minutes with questions.

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SCRIPT

Graphic PVT-1 (Intro Graphic w/Logo)

This presentation on the Premier VI Private Annuity/Trust was produced by The National Association of Financial and Estate Planning (of which I am a member, or which I am affiliated with).

Graphic PVT-2 (Headline - Premier VI Private Annuity/Trust)

The Premier VI Private Annuity Trust has three major uses:

1. Capital gains deferral on the sale of appreciated assets
2. Reduction of taxable estates
3. Medicaid planning, to prevent the loss of your estate from the costs of long term medical care

Graphic PVT-3 (Headline - Premier VI Private Annuity Trust)

Deferral of capital gains taxes is the focus of this presentation.

Graphic PVT-4 (Headline – Capital Gains Taxes on Appreciated Assets)

Capital gains taxes are a tax on the profit we make when we sell assets. The asset may be real estate, personal property, investments and securities, a business, an art collection, etc. Any long term asset sold at a profit is subject to a capital gains tax of some rate. This graphic illustrates this concept. The left side represents the price paid or the cost of the asset. This cost is called the "Basis." Moving to the right side of the graph is a progression thru time. Over time the asset grows in value or appreciates. The right side of the graph represents the point of time at which the owner wants to sell the asset. Unfortunately the seller does not get to keep all the profit, the capital gains, and is taxed at some rate.

The rate for a significantly sized sale of an asset owned for one year or longer (referred to as long term gains) will be 15% for federal taxes. Most states charge 5% to 10% on top of that, making the total tax run as high as 25%. If there is depreciation recapture in the asset sale, that is taxed at 25% federal rate making the tax on recapture higher than the capital gains tax.

Graphic PVT-5 (Headline – Owner Identifies Means of Liquidation)

Prior to the creation of a private annuity transaction, the first step is for the owner of the appreciated assets to identify a means of liquidation. Liquidation will be necessary in order for the private annuity to function properly. And, it won't make any sense to structure a private annuity if there is not some reasonable prospect of liquidating the asset. Liquidation can be done by selling to an outside buyer, selling through the stock markets, etc.

Graphic PVT-6 (Headline – Deferred Taxable Exchange)

The private annuity process starts with a property owner, depicted on the left in this graphic. We will refer to this property owner as the "annuitant" in the rest of this discussion. We are going to use an example in this presentation where we assume that the annuitant owns property worth \$1,000,000, as illustrated in the lower part of the diagram. We know that 1,000,000 is the fair market value because the annuitant previously located a buyer who offered that amount for the property. Before the annuitant enters into a sale with that buyer the annuitant transfers ownership to a trust.

The new owner, the trust, is represented by the bank safe. The owners of the trust are the heirs of the annuitant, probably his children. They are the beneficiaries of the trust. The trust, representing the beneficiaries, becomes the owner of the property once it is transferred to the trust.

Next, the trust "pays" the annuitant for the property. The payment isn't made in cash, but with a special payment contract called a "private annuity." Let me repeat this. The trust purchases the asset from the annuitant. It is very important in understanding this entire program that this is a buy-sale transaction, not a gift to the trust by the annuitant. The form of payment is not outright cash, but is a life annuity.

Graphic PVT-7 (Headline – Annuity Payable for Life)

A private annuity is not an annuity issued by an insurance company. It is strictly a private arrangement between the trust and the annuitant. A private annuity is something like an installment sale. Instead of specifying an exact number of payments as in an installment sale, the private annuity promises to make payments to the annuitant for the rest of his life. The annuity does not have a fixed or a specific term. The payments terminate only at the annuitant's death. The annuity is designed to return all of the annuitant's

principal, \$1 million in this example, with interest. This return of principal with interest is spread out in equal payments over the annuitant's, IRS stated life expectancy. The annuity payments may begin immediately or they may be deferred for some period of months or years.

Graphic PVT-8 (Headline – Non Taxable Sale)

The next step in the private annuity process is for the trust, as the new owner, to sell the property to the previously identified buyer. In the example we are following, the outside buyer pays the trust \$1,000,000 cash for the property, at this point, the private annuity transaction is fully set up. The annuitant sold his property to the trust at fair market value. The form of payment to the annuitant is the lifetime, private annuity. The trust has sold, at fair market value, the property for cash.

Graphic PVT-9 (Headline – Annuity Exchange Not Immediately Taxable)

Now, let's analyze the tax ramifications of this private annuity transaction. First, the ramification to the annuitant is that the exchange is not immediately taxable. Under IRS rules the annuitant is taxed only on payments actually received, as they are received, and not all up-front on the entire amount. This is similar to making an installment sale, then paying taxes only on the installment payments as they are received. If the annuitant chooses to defer his annuity, that is wait for some period of time before payments begin, there will be no taxes during the deferral period because no money is received. Once payments begin, whether immediately or at some deferred period, there will be a proportionate amount of taxes owed on each year's payment. For example, if the annuitant has a 15 year life expectancy, he will owe 1/15th of the total capital gains taxes each year. With a 20 year life expectancy, 1/20th of the capital gains taxes will be owed each year.

Graphic PVT-10 (Headline – Sale From Trust Not Immediately Taxable)

The tax ramification to the trust's liquidation of the asset is zero taxes. That is due to the fact that, in this example, the trust sold the asset for \$1,000,000 to the outside buyer, and the trust paid \$1,000,000 to the annuitant, by means of the private annuity contract. That leaves zero gain to the trust, and zero taxes.

Graphic PVT-11 (Headline – Premier VI Private Annuity Defers & Pays For Life)

This graphic provides a time line illustration of what happens when there is a deferral, and shows the result that our "example" annuitant will receive. This annuitant is 45 years old at the time of the creation of the private annuity transaction, doesn't need the payment and he chose a 20 year deferral. He receives no payments during the 20 year deferral and pays no taxes. At age 65 the payment period begins for the annuitant. At that age the annuitant has a 20 year life expectancy according to IRS tables. During the annuity payment period the annuitant will receive taxable annuity payments for as long as he lives, regardless of whether that is longer than, shorter, or exactly 20 years.

Graphic PVT-12 (Headline – Comparison With A Taxed Sale)

This graphic compares a straight forward, taxed sale (in the left hand column) to the private annuity transaction (in the right hand column). We start with the \$1,000,000 property value. The annuitant's basis is 200,000, leaving a profit or gain of 800,000. We are estimating combined federal and state capital gains taxes at 160,000. This leaves net cash of 840,000 in a direct sale vs. 1,000,000 in the annuity deferral sale.

Next we are assuming in both columns that the net investment cash earns 6.0% on a tax deferred basis (in both columns) for the next 20 years. The property owner or annuitant is age 45 at the beginning, so he

will be 65 when he starts to take payments from either of these plans. Under the direct and taxed sale the property owner receives annual payments of 277,300 vs. 330,119 under the annuity plan. This yields an estimated life payout of 5,546,000 under the taxed plan vs. 6,602,380 with the annuity strategy. That is an advantage of more than one million dollars to the annuitant. This advantage is due to the larger amount of net cash that was initially available to invest for the annuitant.

Graphic PVT-13 (Headline – Tax Treatment Of Each Annuity Payment)

With this illustration we will explain how the annuitant's private annuity payments are taxed. First, this annuitant has a cost basis in his property, and a proportionate share of that basis is returned to the annuitant each year. The basis portion is tax free to the annuitant. Another part of each year's payment will be a proportionate share of the capital gains, and that portion will be taxed at capital gains rates. The last part of the payment is ordinary income, and is taxed accordingly. The reason the annuitant receives ordinary income is that the private annuity always earns interest on the unpaid balance, and interest is paid out each year on top of the basis and capital gains portions.

The proportionate share of tax free return of basis and capital gains is determined by the annuitant's life expectancy at the time that the payments begin. If the annuitant has a 15 year life expectancy, he will receive 1/15th of his basis and 1/15th of the capital gains each year. With a 20 year life expectancy the annuitant will receive 1/20th of basis and 1/20th of capital gains each year. If the annuitant lives longer than life expectancy, he will have received a 100% return of his basis and capital gains at full life expectancy. All further payments will be treated as 100% ordinary income to him. Also note, if the annuitant lives to life expectancy, he will be returned 100% of his investment, with interest. The annuitant gives up nothing by using this strategy.

Graphic PVT-14 (Headline – Depreciation Recapture Comparison With Installment Sale)

While we have primarily focused on the capital gains tax, let's consider depreciation recapture taxes now. As seen in this illustration, depreciation recapture taxes are also deferred with a private annuity. But in either a cash sale or an installment sale the depreciation recapture is taxed immediately. While an installment sale can spread the capital gains out over a number of years, it cannot do the same with depreciation recapture. Furthermore, installment sales have "related party rules" that prevent an arrangement such as the private annuity trust. The related party rules only permit an installment sale to be made with an outsider.

Graphic PVT-15 (Headline - Flexible Trust Investments)

This graphic illustrates the flexibility of available trust investments. The money may be invested in securities and mutual funds, financial instruments such as annuities and V.U.L. life insurance, or real estate. Many investment advisors recommend using the trust funds to purchase either fixed or variable commercial annuities as the best tax advantaged investment vehicle. The trust's investment program is required simply to produce the cash flow necessary for the private annuity payments to the annuitant.

Graphic PVT-16 (Headline - Trustee Choices (1))

Annuitants cannot be the trustee nor have any direct control over the trust. The trustee may be any adult trust beneficiary or any person who is independent of the annuitants. For example, an adult child who is also a beneficiary may be the trustee. The annuitants' accountant, attorney, financial advisor, family friend or a relative who is not in the immediate family are all possible choices. There may be either one trustee, or two co-trustees.

Another trustee option is to use a corporate trustee, which is available through The National Association of Financial and Estate Planning or from a local trust company. With a NAFEP corporate trustee, a co-trustee can be appointed as an extra measure of security or comfort to the annuitants and beneficiaries. Anytime a co-trustee is used, all trust transactions require the signature of both the trustee and co-trustee.

In all cases the beneficiaries have the authority to fire and replace the trustee.

Graphic PVT-17 (Headline - Trustee Choices (2))

If a NAFEP corporate trustee is chosen, the base fee is \$500 per year plus transactional costs. (These are costs for each specific transaction, such as opening a new investment account. In most cases there are few, if any transactional costs after the trust is fully functional.) Using a NAFEP corporate trustee allows an optional benefit of Nevada Domiciling, where state income taxes may be eliminated for the trust.

Graphic PVT-18 (Headline - Benefits To Annuity Property)

Besides deferral of capital gains and depreciation recapture taxes, there are some other benefits to the annuity property.

1. The entire value of the property is removed from the taxable estate of the annuitant. Whatever is left in the trust will pass to the beneficiaries completely free of estate and gift taxes. (If the annuitant dies before receiving all the payments from an installment sale, the balance of the unpaid payments will be in his taxable estate.)
2. The private annuity exchange does not trigger gift tax consequences no matter how much the property is worth. The private annuity is treated by federal tax laws as an arms length buy-sell transaction at fair market value.
3. The property will not need to go through probate when the annuitant dies. None of the property nor any annuity value is left in the annuitant's estate.
4. The property generally will not be subject to Medicaid claims should the annuitant ever require Medicaid assistance with nursing home care. The annuity payments can be subject to Medicaid claims during the life of the annuitant, but in most states the assets in the trust are free of Medicaid claims.

Graphic PVT-19 (Headline – Other Benefits to Annuitant)

The deferral of capital gains taxes can produce a dramatic increase of cash in your pocket. But that is far from being the only benefit from using a Premier VI Private Annuity. Let's discuss some of these other benefits:

1. The family of the annuitant controls the trust and all the money. Everything from the sale proceeds and all trust earnings either goes to the annuitant or to his heirs. When the annuitant dies everything left in the trust will go to his heirs.
2. The trust can make a cash sale. It is not forced to make an installment sale to the outside buyer in order to spread out the capital gains tax. This is an advantage because you never know whether the outside buyer will make all the payments on an installment sale.

3. The private annuity is the equivalent of receiving a tax free loan from Uncle Sam. The \$160,000 of deferred taxes in our earlier example was used to benefit the annuitant for a period that covered 40 years.
4. The formal mechanics of the trust arrangement provide the discipline that some find helpful in their retirement planning. The private annuity works equally well for single or married annuitants. Married couples can have the private annuity written as a joint, last to die contract.

Graphic PVT-20 (Headline – PVT Trust vs. CRT - 1)

A competing strategy to the private annuity is a program known as a “charitable remainder trust” or CRT. In the next few graphics we will compare the private annuity to the CRT. This graphic illustrates that the payment is usually higher with the private annuity. This is due to the fact that the annuity returns all principal with income (interest), whereas the CRT pays only an income stream.

Graphic PVT-21 (Headline – PVT Trust vs. CRT - 2)

Private annuity payments generally receive much more favorable tax treatment. Some of the payment is tax free, some is taxed at capital gains rates and the rest at ordinary income rates. With a CRT, all of the payment may be taxed at ordinary income rates.

Graphic PVT-22 (Headline – PVT Trust vs. CRT - 3)

The private annuity allows much greater flexibility in investment choices. This is due to the fact the annuity is not “qualified,” not regulated by the IRS, whereas the CRT is.

Graphic PVT-23 (Headline – PVT Trust vs. CRT - 4) (needs script, was not in original)

Most private annuity transactions involve real estate, which often has a mortgage on it. Mortgaged property can be used in the private annuity, but it is illegal to use with the CRT. Also, a private annuity can have the beginning of the payment stream deferred, where in most cases that cannot be done with a CRT.

Graphic PVT-24 (Headline – PVT Trust vs. CRT - 5)

A large advantage the private annuity has is that all the benefits stay in the family, where a charity will receive some of the benefits of a CRT. For example, if the private annuity trust earns more money than it needs to make the private annuity payment, that excess may be paid to the beneficiaries at any time. In a CRT there is no such thing as “excess.” Further, when the annuitant dies the family receives all the remainder in the private annuity. With the CRT the remainder goes to the selected charity.

A big problem with the CRT approach is that the annuitant could die early, leaving the family with no further benefits. If the annuitant died right away, as sometimes happens, the entire asset would be lost to the family. To solve this problem, most CRT’s are sold with a life insurance policy on the life of the annuitant. Of course that further reduces the amount of money the annuitant gets from the CRT.

Finally, if in spite of these advantages the annuitant is charitably inclined, the private annuity may still be the strategy chosen, using a charity as the beneficiary of the trust. Then there really is no advantage to the CRT.

Graphic PVT-25 (Headline – Clarifying Common Misunderstandings -1)

There are a few misunderstandings that many people have when they begin looking at the private annuity. One is that the annuitants think they will get their annuity payment, plus anything extra that the trust earns. That is not correct. The private annuity is calculated at the beginning of the process, based on the exchange property's fair market value, plus the interest rate and life expectancy. The calculation yields a fixed, flat payment that will be in effect for the rest of the annuitant's life. The payment never goes up or down. The payment is like a home mortgage payment, it is flat throughout the life of the contract.

Graphic PVT-26 (Headline – Clarifying Common Misunderstandings - 2)

Other misunderstandings which need clarification are:

1. Neither the annuitant nor the spouse of an annuitant can be either trustee or beneficiary. Neither the annuitant nor his spouse can control the trust, and that eliminates the possibility of either being trustee. In some cases the annuitant wants his or her spouse to be the beneficiary so that the spouse gets the trust's remainder when the annuitant dies. But that is not allowed under IRS rules.
2. As we just stated, annuitants cannot control the trust. This means that the annuitant cannot control the trust's investments either directly or indirectly.
3. The annuitant cannot receive any of the excess earnings which may be generated by the trust's investments. The beneficiaries can have the excess, but not the annuitant.

In other words, the annuitant should think of the annuity transaction with the trust as if the annuitant purchased a commercial annuity from a life insurance company. In that case the annuitant could not control the life insurance company, could not direct the insurance company's investments, and could not have any of the earnings of the life insurance company. The private annuity trust must be just as removed from the annuitant.

Graphic PVT-27 (Headline – End Of Presentation)

(Either no narrative needs to be used here, or, depending upon who the presenter is and the circumstances of the presentation use the following:)

The Premier VI Private Annuity program is created and supported by The National Association of Financial and Estate Planning.....