Chapter 24. Life Insurance Trust

If you own Life Insurance and your Estate exceeds the Lifetime Estate Tax Exemption ($5,430,000 each, $10,860,000 if married), then about 40% of your Life Insurance proceeds (over the exemption amount) must be paid for Estate Taxes if you own the Life Insurance policy or if your Estate is the beneficiary. With an Irrevocable Life Insurance Trust ("ILIT"), these taxes can be avoided and your Life Insurance can be fully preserved for your family.

	No ILIT	**With ILIT**
Life Insurance Amount	$1,000,000	$1,000,000
Estate Tax on Insurance	-400,000	-0-
Net After Tax	$600,000	$1,000,000

Why is this? The reason is that if you own the Life Insurance policy or if your Estate is the beneficiary, then the proceeds (face value) of the Life Insurance will be subject to Estate Taxes.

You can avoid this by gifting the policy to someone else or, as to new policies, set up ownership somewhere else (so it's not in your Estate).

But who should you gift it to? Who should own your life insurance? If your spouse owns it, it will still be subject to you and your spouse's Estate Tax. If your children own it directly, then you've defeated the purpose of holding your Estate in trust until they reach certain ages. Plus, if they own it, the proceeds can't easily be used for the benefit of your surviving spouse. If your Living Trust owns it, the proceeds will still be subject to Estate Tax.

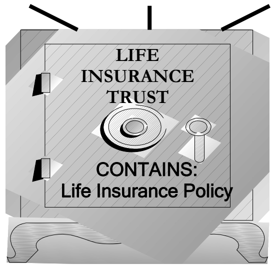
The most frequently used solution is to sign a Life Insurance Trust. This is used to avoid Estate Tax on your life insurance. This Trust will have provisions essentially the same for holding and distributing to your children, and it also holds the funds for the benefit of your surviving spouse.

The Life Insurance Trust needs to be both the owner and beneficiary of the life insurance policy (and should also be the policy applicant for new policies). Premiums are paid with funds that you annually place in the trust. If you provide certain specific withdrawal rights to the trust beneficiaries (e.g. your children), then the premium payments can qualify for your Annual Exemption Gifts.

To be tax-effective, the Trust itself needs to be irrevocable because it in essence is a gift of the policy to your beneficiaries. However, the Trust has enough flexibility that this typically poses no problem.

Life Insurance Trust

Parent **Trustee** **Family**
(Spouse & Kids)



Distributions to Family as Needed or Per Times Set In Trust

BENEFITS

- **Estate Tax Savings**

EXAMPLE:

$1,000,000 Life Insurance

Estate Tax without Trust:	**$400,000**
Estate Tax with Trust:	**-0-**
SAVINGS	**$400,000**