

ESTATE planning | Life Insurance Trusts

Life Insurance Trusts

Few people realize that even though they may have a modest estate, their families may owe the government hundreds of thousands of dollars because they own a life insurance policy with a substantial death benefit. This is because life insurance proceeds, while not subject to federal income tax, are considered part of your taxable estate and are subject to federal estate tax up to 55%.

The solution to this problem is to create an irrevocable life insurance trust to own the insurance and receive the policy proceeds on your death. A properly drafted, implemented, and maintained life insurance trust keeps the insurance proceeds from being taxed in your estate as well as in the estate of your surviving spouse. It can also protect the trust beneficiaries from their own “excesses” against their creditors and in the event of divorce. Moreover, the trust can also provide reliable management for the trust assets. Here’s how a life insurance trust can work.

You create a life insurance trust to be the owner, beneficiary, payor, and beneficiary of one or more life insurance policies on your life. You contribute cash to the trust to be used by the trustee to make premium payments on the life insurance policies. The contributions you make to the trust for premium payments can generally qualify for the annual gift tax exclusion. The life insurance trust typically provides that during your lifetime, principal and income, in the trustee’s discretion, may be paid or applied to or for the benefit of your spouse and heirs. This allows indirect access to the cash surrender value of the life insurance policies owned by the trust, and permits the trust to be terminated if desired despite its being irrevocable. On your death, the trust continues for the benefit of your spouse during his or her lifetime. Your spouse is given certain beneficial interests in the trust, such as entitlement to income, limited invasion rights, and eligibility to receive principal. On the death of your spouse the trust assets are paid outright to, or held in further trust for the benefit of, your descendants.

If you own a life insurance policy with a significant death benefit, an life insurance trust may be of substantial benefit to you.

*The purpose of this document is to provide general information, not legal advice. A qualified attorney should be consulted before implementing any plan.



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