



THE VALUE OF LIFE INSURANCE TRUSTS

An estate planning option more families ought to know about.

You may think of life insurance in very simple terms: you buy a policy so that your loved ones will have some financial assistance when you die. But if you have substantial assets, you should view life insurance as a tool - kind of a Swiss army knife, in fact. Life insurance has many potential uses in estate planning, and an irrevocable life insurance trust (ILIT) can certainly help a family.

What does a life insurance trust do? It enables you and your family to do three things in particular. One, it provides you, your spouse and your heirs with life insurance coverage after it is implemented. Two, it allows a trustee to distribute death benefits from a life insurance policy as that trustee sees fit. Three, it gives you the chance to reduce your estate taxes.

When you create a life insurance trust, you are creating an entity (the trust) to buy life insurance policies for you and your loved ones. You don't own the policies, the trust does. So the insurance proceeds go into the trust when someone passes away. Because the trust owns the insurance policies instead of a person, the insurance proceeds aren't subject to probate, income taxes or estate taxes. The trustee can distribute those proceeds to one or more parties as stipulated in the language of the trust. Also, if your estate ends up really large, the trust can buy additional life insurance to provide additional cash to pay additional estate taxes.

Sometimes these trusts establish investment policies for life insurance proceeds, and even timelines for who receives what when (families may want to delay an heir from legally receiving an inheritance until age 18 or 21, for example).

Why not just have someone else own my insurance policy? That scenario can lead to major financial and familial headaches. If that person dies before you die, the cash value of the policy will be included in their taxable estate. So the heirs (and relatives) of that person will have higher estate taxes to pay as a result. Also, if you do this, you surrender control of your policy; the loved one you trust could end up naming another beneficiary or even cashing your policy out.

A decision for life. These trusts are irrevocable. That is, they are legally "set in stone" once created, unlike a revocable trust which can be amended or revoked after creation. You can make these trusts revocable, but if you do, you lose the tax benefit: the insurance proceeds will be included in your taxable estate when you die, which could increase the estate tax bill for your heirs. However, some irrevocable life insurance trusts purchase survivorship life insurance in a profit sharing plan to permit the ability to change beneficiaries.

If you'd like to know more about life insurance trusts or the potentially significant changes in estate taxes over the next few years, talk to a qualified legal, financial or insurance professional today.

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