IRREVOCABLE LIFE INSURANCE TRUST

Personal life insurance policies are widely used to provide financial security for a family in the event of a death. Unfortunately, life insurance proceeds are generally includable in the gross estate of the policy owner and are, therefore, potentially subject to estate tax. To avoid including the insurance proceeds in the estate of either spouse, the owner of the policy can employ an estate planning tool known as the irrevocable life insurance trust. An irrevocable trust is established to own the policy and pay the premiums. The grantor (the person establishing the trust) makes annual gifts to the trust to provide the funding for the premiums. If structured properly these annual gifts can qualify for the $10,000 annual exclusion. When the insured dies, the proceeds are paid to the trust and are not included in the grantor's taxable estate. The surviving spouse can receive all of the income from the trust, and the trustee can be authorized to make principal distributions in the event of hardship or medical needs.

The trust works best with the purchase of new policies, but existing policies can also be used. However, if an existing policy is used and death occurs within three years of the transfer, then the value of the policies must be included in the estate. Although not for everyone, particularly those with estates under $625,000, the irrevocable life insurance trust should not be overlooked in your estate planning.