INSURANCE

What You Might Not Know About Life Insurance

By Kira S. Masteller

Many people own life insurance so that their family will have sufficient capital for a specific period of time. Others own life insurance to enable a business partner to buy out the family's interests upon their death. Still others have life insurance specifically to pay estate taxes.

The problem arises when you are the Owner of the policy. If you own life insurance, the death benefit of the insurance will be included in your estate for estate tax purposeswhen you pass.As an example, your home, savings and retirement benefits may not comprise a taxable estate – until you add a $1,000,000 death benefit.

An irrevocable life insurance trust can help you avoid creatinga tax, if you set it up to own your life insurance.

You may not be the Trustee of the trust. You must appoint a trusted family member, friend, or a professional Trustee. The Trust will own the life insurance policy, and the Trustee will pay the premiums annually (which you will gift to the trustee each year). The Trustee will file a claim upon your death and receive the insurance proceeds available for your family, or pay the estate tax as you planned.

Not only can life insurance trustsprevent the creation of a taxable estate, they also provide liquidity to an estate that is already taxable. Singleswith estates valued above $5,120,000 may purchase life insurance to pay estate taxes so that the full value of their estate can pass to their beneficiaries. Assets will not have to be sold to pay taxeswhich will be due nine months after the death.

Couples with estates that are valued at more than $10,240,000 may also purchase survivorship life insurance which does not provide a death benefit until both spouses have passed away -- again to provide liquidity at death to pay estate tax due nine months after the death of the surviving spouse.

Many believe that life insurance is tax free at their death. While part of this may be true (beneficiaries will not have to pay income tax on the monies received), life insurance is included in the insuredperson's estate. Often life insurance will actually create a tax that would not have otherwise existed for the insured.

Because a life insurance trust is irrevocable, people are leery of creating a trust they cannot change. The solution to the issue of irrevocability lies in the drafting of the trust. Language can be included to allow for trustee and distribution provisions to be changed by a Trust Protector (an individual appointed by the Grantor of the Trust who has the limited ability to change these specific provisions) while still conforming to the rules required to be a valid life insurance trust.

You can utilize a Life Insurance Trust for the benefit of yourchildren which also provides the "what if" provisions providing for a spouse as a beneficiary, or to change distribution provisions for a child who is not mature enough to receive assets at the age initially provided in the trust.

A successful estate plan includes planning for the goals of yourfamily, each of your unique assets, and tax issues, withoutcreating an unnecessary estate tax.

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