

SWEET & MAIER, S.C.

Irrevocable Life Insurance Trust Agreement

An Irrevocable Life Insurance Trust is a useful, but somewhat complicated, estate planning tool. Essentially, the Irrevocable Life Insurance Trust is a trust that is created to own one or more life insurance policies so that the value of those policies will not be included in the estate of the individual for purposes of assessing estate tax liability.

Ownership of the insurance policy funding the trust will be titled in the name of the trust. The individual will then make “gifts” to the trust in amounts roughly equal to the annual premiums owing on the policy. The trustee will then use those contributions to pay the annual premiums and keep the life insurance policy in force. The trust will also be named as the beneficiary of the life insurance policy or policies. The trust document will therefore contain specific instructions for the distribution of the payout amount of the life insurance policy upon the death of the insured.

Primary Benefit

Thus, the primary benefit to be realized by the implementation of an Irrevocable Life Insurance Trust is that it allows an individual to leave a significant financial benefit to one or more named individuals (i.e. your children) without that amount being included in the individual’s estate for estate tax purposes. It will be, of course, necessary to coordinate the distribution provisions of the Trust with your other estate planning documents so that a uniform and acceptable distribution plan will be realized through all of your estate planning documents.

Gift and Estate Tax Issues Presented

Although the reduction of estate taxes is a primary concern, another issue to be aware of is the possible assessment of gift taxes. More specifically, one of the objectives in forming an Irrevocable Life Insurance Trust is to draft the agreement in such a way that the premiums to be contributed to the trust can be done so with minimal gift tax implications.

One of the mechanisms for avoiding or at least reducing gift tax liability is to make full use of the “annual gift exclusion” provided to you under the Internal Revenue Code. Presently, you are entitled to gift up to \$14,000 per year per donee with no gift tax liability as long as the gift is deemed a gift of a present interest. In order to qualify a contribution to the trust as a gift of a “present interest”, it is necessary to provide each beneficiary with notice that he or she technically has the right to withdraw all or a portion of that contribution. Although it is anticipated that the beneficiary will never exercise that right, the simple fact that the beneficiary is notified of this right of withdrawal will qualify the contribution as a gift of a present interest.

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Therefore, one of the administrative functions that must regularly occur is the notification of beneficiaries of any trust contributions. Because this notification is essential to the utilization of the annual gift tax exclusion, it is important to ensure that the trustee will carry this function out on a regular basis. For this reason, we often recommend that a knowledgeable, professional, or Trust Company, be named as trustee since they have the physical systems and capabilities to provide these notices on a timely basis.

There are other more complex issues which often arise in the preparation of Irrevocable Life Insurance Trust Agreements which our attorneys are prepared to address and handle. Additional detailed information on these specific issues is available for you at your request.

Frequency of Premium Payments

One of the decisions you will have to make with respect to the insurance policy or policies to be purchased to fund the trust, is the frequency in which premium payments will be made. Generally, you can choose to pay premiums monthly, quarterly, bi-annually or annually. It is our recommendation that you set up the insurance policy so that the premiums are due on an annual basis. We recommend this for a couple of reasons. First of all, this option will generally be the most attractive from an economic standpoint as the actual amount of premium payment decreases as the frequency of the payment decreases. Therefore, by paying the premiums on an annual basis rather than quarterly or monthly, you will actually end up paying fewer premiums. In addition, this will greatly simplify the administrative responsibilities of the trustee. As indicated above, the trustee is required to send out a notice to the beneficiary or beneficiaries of the trust each time a contribution is made to the trust. By paying premiums annually, and thus making only one annual contribution to the trust, the trustee will only be required to send out one notice a year.

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