Buskey Law Offices

Lynn A. Buskey, JD, MBA
LL.M. in Estate Planning
Admitted in MA & FL

101 Federal Street
Suite 1900
Boston, Massachusetts 02110
www.BuskeyLaw.com

Tel: 617-447-2330
Fax: 617-447-2367
Lynn@BuskeyLaw.com

Life Insurance Planning

The estate tax laws that apply to life insurance are, in my humble opinion, absurd. The best way to describe the problem is with examples:

- Example 1: You purchase a $2 million life insurance policy on your life. The policy is owned by you. When you die, the $2 million is paid out to your estate planning trust (for your spouse's benefit and then the children). Your estate tax return must report the $2 million death benefit as part of your taxable estate, and it is taxed at the regular estate tax rates. This means that your $2 million policy could provide a net benefit of about half that after federal (up to 40%) and state (up to 16%) estate taxes.

- Example 2: You create an irrevocable life insurance trust (ILIT). The trustee of the ILIT purchases the policy (or you transfer ownership of an already purchased policy to the ILIT). When you die, the death benefit is paid to the ILIT as beneficiary. We inform the taxing authorities that this policy existed and paid out the death benefit, but it is <u>not</u> subject to estate tax. Your family receives the full $2 million death benefit free of taxes via the ILIT. NOTE: if you transfer the policy by gift to the ILIT there is a three-year waiting period before the death benefit will not be taxed in your estate. Of course, there are planning options to address this risk, but they are beyond the scope of this memo.

It is difficult to explain how some relatively simple planning can make such a difference in the outcome, but unfortunately for many it is simply a tax trap. The ILIT could also offer the additional benefits of asset protection for your family, as well as the exclusion of the death benefit from the surviving spouse's estate and even the children's estates.