Deutsche Bank
Wealth Management

Irrevocable life insurance trusts

An irrevocable life insurance trust (ILIT) is a trust that a donor creates during life for the benefit of one's heirs or spouse and chosen beneficiaries. In general, an ILIT owns insurance on the life of the donor (or donors for second-to-die insurance policies).

On the death of the donor, or the second-to-die of the donors, the insurance proceeds pass, assuming that the document or the trust agreement is properly structured, without imposition of any estate transfer taxes. This is because the donor(s), now the decedent, did not "own" the insurance within the definition of estate tax laws. For example, if an individual, and if married, the spouse, create an ILIT, the trust's main asset, the insurance proceeds, will pass outright to the beneficiaries of the donor(s) free of transfer/inheritance tax.

There are, of course, other issues that need to be addressed prior to creating and funding an ILIT, such as insurance premiums, annual gifts, lifetime gift taxes, as well as overall estate planning strategies.

Benefits

- Estate conservation: The ILIT can provide family members and heirs with a source of liquidity to pay estate taxes and thereby conserves the estate upon the insured's death.
- Estate creation: The ILIT can create an immediate source of wealth for the decedent's heirs.
- Estate equalization: The ILIT, by conserving and creating liquid wealth, can ensure that the decedent's estate is distributed equally and that each heir is treated fairly. This is particularly useful when most of the decedent's estate is comprised of illiquid assets, difficult to be evenly divided among beneficiaries.
- The ILIT should receive any insurance death benefits free of federal income tax.
- Trust assets, including any appreciation, generally will not be includible in the donor's estate and will grow inside of the trust free of federal estate and gift taxes.
- Trust distributions generally can be made to beneficiaries free of federal estate and gift taxes.
- The ILIT can be structured so that contributions to the trust (which the trustees will primarily use to pay for insurance premiums) will qualify for the federal annual gift tax exclusion by giving trust beneficiaries certain rights (sometimes referred to as a "Crummey Power") to withdraw these contributions.
- Trust assets may be protected from beneficiaries' creditors (e.g. ex-spouses).

Considerations

- ILIT assets will only be available to trust beneficiaries as provided in the trust document.
- As an irrevocable trust, the donor cannot decide to terminate the trust and take back the trust assets after the trust is funded.
- If the donor transfers to the trust any existing life insurance policies, the donor must live three years thereafter or any such policies will be subject to federal estate tax at the donor's death.

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