Consider your options when addressing life insurance in your estate plan

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Life insurance has long provided a source of liquidity to pay estate taxes and other expenses. Even though for many families, federal and state estate taxes aren't a concern, life insurance continues to offer many benefits for these nontaxable estates. For this reason, it's important to properly account for your life insurance policies in your estate plan.

Who should own the policy?

If you own life insurance at your death, the proceeds will be included in your taxable estate unless you take certain steps. Ownership is usually determined by several factors, including who has the right to name the beneficiaries of the proceeds. If estate taxes are a concern, the way around this problem is to not own the policy when you die. However, don't automatically rule out your ownership either.

To choose the best owner, consider why you want the insurance. Do you want to replace income? Provide liquidity? Or transfer wealth to your heirs? And how important are tax implications, flexibility, control, and cost and ease of administration?

Here are four possible owners:

1. **You or your spouse.** There are several nontax benefits to your ownership, primarily relating to flexibility and control. The biggest drawback is estate tax risk. Ownership by you or your spouse generally works best when your combined assets, including insurance, won't place either of your estates into a taxable situation.
2. **An ILIT.** A properly structured irrevocable life insurance trust ("ILIT) could save you estate taxes on any insurance proceeds. The ILIT owns the policy and pays the premiums. When you die, the proceeds pass into the ILIT and aren't included in your estate. The ILIT can be structured to provide benefits to your surviving spouse and/or other beneficiaries.
3. **Your business.** Company ownership or sponsorship of insurance on your life can work well when you have cash flow concerns related to paying premiums. Company sponsorship can allow premiums to be paid in part or in whole by the business under a split-dollar arrangement. But if you're the controlling shareholder of the company and the proceeds are payable to a beneficiary other than the business, the proceeds could be included in your estate for estate tax purposes.
4. **Your children.** Ownership by your children works best when your primary goal is to pass wealth to them. On the plus side, proceeds aren't subject to estate tax on your or your spouse's death, and your children receive all of the proceeds tax-free. On the minus side, policy proceeds are paid to your children outright. This may not be in accordance with your estate plan objectives and may be especially problematic if a child has creditor problems.

Turn to us for help

Please contact us if you're planning to include life insurance in your estate plan but are unsure of the best way to do so. We can help you determine who should own the policy given your specific circumstances.

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