

## ILITs – A Physician's Gift to Securing Your Wealth

With the limited free-time you have outside of work, drafting a sound estate plan is usually not the first thing on your list of chores. However, a simple overlook can cost you money. When discussing an estate plan, more and more physicians have begun to inquire about Irrevocable Life Insurance Trusts (ILIT). An ILIT is a unique estate planning tool utilized to help minimize taxes – estate or gift, by reducing the size of their estate.

This trusted tool has saved physicians hundreds, if not thousands of dollars by limiting the amount of taxes their estate has paid upon their death. Although common amongst medical professionals, many still hesitate to implement this tool as part of their overall estate plan. In this newsletter, physicians will learn the benefits of creating an ILIT and why it should be part of your overall estate plan.

### Life Insurance Policies are Protected from Creditors

With the ever-changing demands of society, it has become essential for every physician to carry some form of life insurance to ensure your loved ones are taken care of after you pass. The amount of coverage varies depending on the family and your current lifestyle. However, there is no dispute that carrying life insurance is no longer a luxury, but rather a necessity.

Life insurance is still considered one of the most important tools to have when discussing your estate and asset protection plan. However, many physicians have questioned whether the life insurance policies are protected from creditors.



The answer can be found in MCL 500.2207(1), which, in relevant part, states:

*“It shall be lawful for any husband to insure his life for the benefit of his wife, and for any father to insure his life for the benefit of his children... free from all claims of the representatives of such husband or father, or of any of his creditors ...”*

Nevertheless, despite the obvious protection physicians receive, having a sole policy without further planning can prove to be disadvantageous to your overall estate plan. Many physicians fail to take into consideration the tax ramifications life insurance can have on their overall estate.

## DID YOU KNOW YOUR LIFE INSURANCE PROCEEDS ARE SUBJECT TO FEDERAL ESTATE TAXES?

Many physicians are unaware that without proper planning life insurance proceeds become subject to federal estate taxes. This is something often overlooked until you realize the sizable amount of estate taxes you pay. For example, if a physician has an estate valued at \$6 million, under the current laws where \$5 million is exempted, \$1 million is subject to taxes. Therefore, \$350,000 will be unnecessarily paid to the government in taxes. If you were to have a \$1 million life insurance policy as part of that estate, then you could save that \$350,000 by implementing an ILIT.

The State of Michigan includes life insurance proceeds in your estate if you claim "incidents of ownership" over the policy; for example, being able to change your beneficiary; borrow from your policy; or exercise any other right that is usually possessed by an owner. By giving up these rights you are assured to have your proceeds excluded from your estate.

Another option is to list your spouse as the beneficiary. This too, reduces the value of your estate, as the proceeds will be excluded, but don't be fooled into thinking the planning stops here. What happens when your spouse passes away? The amount your spouse inherited will be counted in his/her estate. Therefore, although you possibly avoided estate taxes upon your death, you have not completely solved the problem. This is where the effectiveness of an ILIT is best illustrated.



### ILIT BENEFITS:

- Reduces your estate
- Ensures security for loved ones
- Ensures creditor protection
- Reduces estate taxes for yourself and your spouse
- Protects from beneficiaries' creditors gaining access to inheritance



**“An ounce of prevention is worth a pound of cure.”**

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## HOW DOES AN ILIT WORK?

The contributions you make to your trust are viewed as gifts that are used to pay the premiums. All "gifts" made to the trust must take the form of present interests gifts, meaning a beneficiary of the ILIT must have immediate access to the gift.

However, when you make your contributions/gifts to the trust, it does not qualify as a present interest gift. That is where the Crummey Letter steps in. A Crummey letter converts your gift into a present interest gift. Each year, the trustee of the trust is required to submit a Crummey letter to each beneficiary indicating that a gift to them has been made. Once a certain period has lapsed, your gift becomes a present interest gift, therefore, reducing your estate.

Once your trust is created, you have the option to transfer existing policies, or have the trustee apply for a new policy. The benefit of [www.website.com](http://www.website.com) applying for a new policy is that the “three-year rule” will not apply. The “three-year rule” is when you transfer an existing policy into your trust and you don’t survive for three years from the date of transfer, then the proceeds will be included in your estate. However, under a new policy, the proceeds would be excluded.

An ILIT is an extremely useful tool used by many physicians to help minimize their estate taxes. With the estate tax exemption being widely speculated to hit pre-2001 figures, \$1 million exemption at a 55% tax rate, ILITs are increasingly becoming the most popular estate planning tool. Remember, planning for today will serve you no protection for tomorrow; but planning for tomorrow will serve you protection for today.