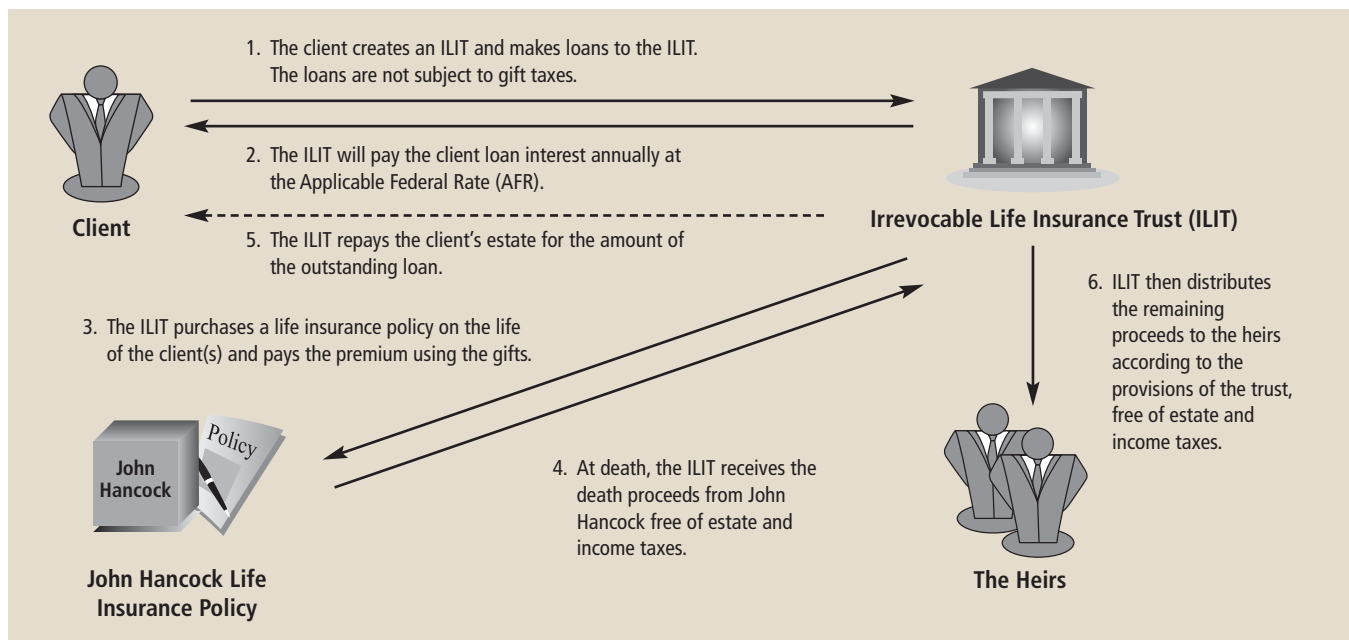


How Does It Work?

- The client creates an Irrevocable Life Insurance Trust (ILIT) which will apply for a life insurance policy on his/her life, or the lives of both spouses.¹
- The client enters into a loan agreement with the ILIT where he/she lends money to the trust to pay the premium.²
- The ILIT will owe the client loan interest based on the current AFR, which may either be paid annually or deferred and added to the total loan amount. The loan may be repaid from the policy proceeds at death, or earlier from other sources, such as trust side funds.



Benefits

- Gift taxes may be eliminated or significantly reduced since the gift is only the loan interest and not the full premium.
- The heirs, in many cases, receive the loan repayment net of estate tax.
- No approval by a third party is needed and the trust does not have to post collateral to secure the loan. There is also no risk of the loan being called by a third party lender.

Considerations

- The client must have enough cash flow or liquid assets to pay the full premium or make a lump sum cash loan.
- The loan repayment may be subject to estate tax if the client is the lender.
- If an existing trust is the lender, it must pay income tax on the loan interest it receives from the ILIT.



1. Trusts should be drafted by an attorney familiar with such matters in order to take into account income and estate tax laws (including the generation-skipping transfer tax). Failure to do so could result in adverse tax treatment of trust proceeds.
2. The lender could also be a Family Limited Partnership (FLP), Limited Liability Company (LLC), or another existing trust. The loan can be made annually or in an up-front lump sum to create a sinking fund (to cover future premium and interest payments) or to provide the trust funds to purchase an income producing asset.

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