Insurance: A Major Estate Planning Tool

Insurance is at the bedrock of estate planning. First, it reduces the risk of your estate being wiped out by unforeseen events. Second, it has unique characteristics that allow for sophisticated planning.

Q.: What types of insurance should I consider?
A.: You should consider:

• Insurance on you:
Life insurance pays a death benefit to your beneficiary. This is an essential insurance for someone who has responsibilities, such as a family, but has not yet built enough resources to cover those responsibilities in the event of a premature death. Disability insurance provides you with income if you can no longer work. Health insurance pays for medically necessary procedures and medications for you.

• Insurance for your home:
Title insurance protects you against the possibility of someone claiming that your home is actually theirs. Homeowner's insurance covers the risk of fire or other damage to your residence. It also covers the contents of your home and liability to third parties who are injured in your home. A renter's policy covers only the contents of the rented property and third-party injuries. Typically, earthquakes and floods are risks that are not covered and require separate policies for protection.

• Other insurance:
Auto, boat, and other types of "umbrella" insurance protect both the property and/or any liability that arises from your use of that property. Umbrella coverage goes on top of the other types of coverage. For example, if you have a $1 million umbrella and are in an auto accident, the claim would first go through your auto coverage (let's assume $250,000) and then your umbrella. Umbrella coverage also covers negligence for actions you may take that are unrelated to your home, auto, etc.

Q.: How can insurance help in estate planning?

A.: The various types of property insurance preserve what you have built by protecting against losses from the destruction of the property and from liability that may arise from their use or ownership.

Life insurance can also be an excellent asset for use in estate planning because, while it has little value during your lifetime, it has great value at your death. For example, assume you want to pass down $5 million to your descendants. If you purchased a $5 million term policy with a 20-year level premium, you would pay around $10,000 per year if you were 50 years old. If you set up an irrevocable trust and have the trust buy the insurance policy, it could be free from taxation at your death. (If you do not buy the life insurance policy through a trust, you would owe more than $1 million in estate taxes at your death, assuming you died owning $5 million in life insurance, and even if you had no other assets.) The only taxable transfers to the trust would be the contributions for the premiums. However, even those premiums could be gift-tax free. Thus, purchasing life insurance through a trust is a simple way to get a great many assets to the next generation tax free.

Q.: Who can help me figure out how to use insurance to help in estate planning?
A.: A qualified estate planning attorney can help you minimize your risks and accomplish your goals for you and your beneficiaries.

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