USING YOUR RESIDENCE TO REDUCE ESTATE TAX

If you are in the top estate tax bracket, 55% of your net worth will go to the Federal Government at your death. Estates over $600,000 are subject to tax rates that start at 38%. Proper planning for the transfer of the wealth that you have accumulated during your lifetime is critical.

One of the most common estate planning strategies is to make gifts to family members. Unfortunately, many people are not at a point where they can afford to gift income producing property. The ideal gift would be an asset that is not producing income, appreciating rapidly, and is something that you would like to see kept in the family. A ***Qualified Personal Residence Trust (QPRT)*** may be an effective planning tool in this situation.

The basics of this planning strategy involve your primary and/or secondary residence. Vacation homes can be a great asset to use, but they cannot be rental properties. You transfer ownership of the residence to an irrevocable trust, but retain all rights and use of the property for a period of years. At the end of the trust term, your free use of the residence is up, and you have several options. These include to stop using the residence, rent the house from the beneficiaries, or buy the residence back. You do have to live past the end of the trust term to make this strategy work.

The real benefit of this planning strategy comes from the ability to ***"leverage"*** your gift today. The current value of the house is reduced by the value of your retained interest. You also remove any future appreciation on the residence from your estate. Today's gift could be quite small in relation to the future value that is removed from your estate.

For example, let's assume you are 71 years old and you have a residence valued at $650,000 today. If you set up a 10 year QPRT, the value of the gift you make today is less than $200,000. This would use up part of your lifetime exemption (the $600,000 amount that is sheltered from estate tax), but would remove $450,000 of value from your estate. If the residence appreciates at 4% over that 10 year period, your family saves over $407,000 of estate tax!

The QPRT is just one of the numerous estate planning strategies available. As always, you need to focus on your family's goals in this area to see if it is appropriate. It will also be important to continue to watch potential changes to the estate tax rules over the coming months.