FPA FINANCIAL PLANNING PERSPECTIVES

It's Time to start thinking About the Estate Tax Again

Back in 2001, the Economic Growth and Tax Relief Reconciliation Act triggered a gradual increase in the dollar threshold of estates subject to the estate tax. In tax years 2007 and 2008, estates valued at more than $2 million may be taxed as much as 45 percent, while in tax year 2009, the threshold will increase to $3.5 million. The year after that, the tax will be repealed for a year.

However, in 2011, unless Congress acts, the party's over. The estate tax will be reset at up to 55 percent on estates at a significantly lower threshold – $1 million.

While bills continue to swirl around Congress and many expect a Band-Aid of some sort before 2011, no one seems to believe that the so-called "death tax" is likely to be eliminated altogether. That makes it tough for individuals to set a clear course for their own estate planning. If you suspect your estate or the estate of relatives you might inherit from may fall prey to the estate tax, it makes sense right now to enlist the help of experts. Assets may be expected to grow over time, and your estate may turn out to be larger than you may think. You should be talking to estate and tax specialists as well as financial advisors such as Certified Financial Planner™ professionals.

Here are some things to keep in mind as you plan those conversations:

Think about a life insurance trust: Whether you need it for estate liquidity or for other purposes, an irrevocable life insurance trust can be created to keep the proceeds of the insurance out of your taxable estate. An added benefit is that such trusts may permit spousal access to the cash value of the policy. Yet note the word "irrevocable" – it means a decision that cannot be changed.

If your assets are expected to increase: A grantor-retained annuity trust, or GRAT, is an irrevocable trust that is popular among families with assets that are expected to increase, because such appreciation can be passed on to heirs with minimal tax consequences.

Prepare a gifting strategy: Under current law, unlimited amounts can be left to a spouse or to charity free of federal estate tax. Other heirs can receive a total of $2 million, tax-free, when deaths occur in 2007 or 2008. If your assets are over the estate tax limit, it might make sense to devise a gifting strategy that spends down your total taxable estate while still allowing you a comfortable lifestyle. You might, for instance, consider making direct payments for someone else's medical bills or education tuition. No gift tax applies for these items, so payments can be unlimited.

January 2008 — This column is produced by the Financial Planning Association, the membership organization for the financial planning community, and is provided by Marnie Aznar, MBA, CFP®, a local member of FPA.