Year-end Estate Planning

By Jane Higgins

Before the end of 2007, here are some estate planning suggestions to review:

Review Your Current Estate Plan: This should be done at least every 3-5 years, but if you have gotten married or divorced, had or adopted a child, or experienced some other life-changing event recently, you should adjust your plan sooner. Receiving an inheritance, buying life insurance, or otherwise increasing your assets, may also warrant adjusting your estate plan now.

Currently, each individual is entitled to a tax credit against federal estate taxes, which enables $2,000,000 (the "applicable exclusion amount") to pass tax-free. This amount will increase to $3,500,000 in 2009 and will be unlimited in 2010. However, in 2011, barring Congressional action, the applicable exclusion amount is set to revert to $1 million. Assets over the applicable exclusion amount are subject to federal estate tax at 45%, and when combined with Ohio estate taxes, the tax paid can be as high as 52%. For married couples, the estate of the first spouse is en-titled to a deduction for all property transferred at death to the surviving spouse tax-free. However, at the surviving spouse's death, all assets passing to non-charities are subject to estate tax, payable 9 months following death. The best ways to reduce or eliminate estate tax require advance planning.

Most importantly, if you do not already have an estate plan, identify a lawyer who can develop a customized plan. You should discuss the following with your lawyer:

- What happens if I die without a will?
- What happens if I am unable to make medical decisions for myself?
- What happens if I am temporarily or permanently unable to manage my personal affairs?

Annual Exclusion Gifts: Gifting is an excellent way to reduce your taxable estate. You may make gifts of up to $12,000 per year per individual ($24,000 per year per individual, if you are married and gift-splitting) without being subject to gift tax. Larger gifts are subject to gift taxes; however, the excess, up to the gift tax lifetime exclusion amount of $1 million, may be made without any actual payment of gift tax. Gifts exceeding the lifetime exclusion amount will be taxed at the highest estate tax rate, except for 2010, when the rate will match the highest individual income tax rate.

Where are the savings? If your estate is currently in the 45% federal estate tax bracket (which applies to every dollar over $2,000,000 subject to estate tax at death), 45¢ of every dollar will pay federal estate taxes at your death, but for every dollar you give away during your lifetime, you will save 45¢ in federal estate taxes.

Gifting property means that the property is removed from your taxable estate (as is its future appreciation), plus the income from the gifted assets can be shifted to lower-bracket taxpayers. Keep these points in mind when making gifts: first, if you gift-split with a spouse or make gifts in excess of the annual exclusion limitations, you must file a gift tax return. For 2007 gifts, that return is due April 15, 2008. Second, gifts made by personal check near year-end must be received and cashed on or before December 31st.

Advance Tuition and Medical Payments: Payment of tuition directly to the educational institution is not a taxable gift and is not applied to the annual exclusion limit. Direct payments to a medical-care provider for an individual's medical expenses also qualify as non-taxable gifts which are not subject to the annual exclusion limit.

Establish or Contribute to a 529 College Savings Account: Most states sponsor Section 529 plans, such as Ohio's CollegeAdvantage Plan. Participating allows donors to invest up to $306,000 per beneficiary in selected mutual funds, and, thanks to provisions in the tax code, these funds grow tax-free for the benefit of the beneficiary. The money invested in the funds may be used for a beneficiary's tuition, room, board, books and other qualified college expenses at any accredited college in the country.

To participate, the account owner or the beneficiary must be an Ohio resident. Once the account is open, anyone may contribute money to it. Donors may give up to $12,000 per beneficiary each year without incurring gift tax (for those making larger gifts, donors can accelerate 5 years of gifts into one by giving up to $60,000 per beneficiary in one year without triggering gift tax and pro-rating the gift over 5 years).

An account may have only one beneficiary, but the ac-count owner can change the beneficiary to another child or family member (i.e., if the beneficiary doesn't go to college, drops out, or finishes college without using the full amount). The account owner controls the distributions even after the beneficiary reaches 18.

Withdrawals taken by a beneficiary but not used for qualified education expenses are taxed at the beneficiary's tax rate and are subject to an additional 10% earnings penalty. The money may be withdrawn penalty-free if a beneficiary dies or becomes permanently disabled, although income tax will still be owed on the earnings.

Ohio residents may take a deduction of up to $2,000 for contributions to Section 529 plans, per beneficiary, on their Ohio income tax returns. For contributions above $2,000, the donor may carry the rest of the deduction forward into future years.

For more information on year-end tax planning strategies, please contact Jane Higgins or your CPM attorney.