CLIENT **BULLETIN**

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Estate Planning Update for 2006

Although spouse beneficiaries are able to inherit any amount of property through the unlimited marital deduction, leaving everything to a spouse is not always the best estate planning move. More of your IRA and other assets can now pass free of estate tax to non-spouse beneficiaries such as your children or grandchildren. That goes especially for couples whose net worth is larger than $2 million. While one might think $2 million is a high number to reach, these days it is not when one includes the value of house(s), investments and life insurance.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) changed many tax rules, and it's being phased in through 2011. For 2006, the estate tax exemption has been increased to $2 million, where it will remain for the next three years. A married couple now has $4 million of protection from estate taxation, provided that their wills or trusts are set up to take advantage of each spouse's $2 million exemption. This rule change should eliminate estate tax for millions of families that would otherwise have been subject to it. As a result, larger amounts of your estate can now be passed to children and other beneficiaries, tax-free.

So what should you make sure to do, if you think your taxable estate might be approaching or exceeding $2 million? A major goal of your estate plan should be to ensure that both you and your spouse avail yourselves of the applicable federal estate tax exemption. Married couples can take one exemption amount for each spouse, thereby doubling their protection from federal estate tax. Most married couples, however, waste their first exemption, because they leave everything to each other, through a simple will and accounts that are titled JT TEN (i.e. joint tenancy with right of survivorship). If your net worth exceeds the exemption amount, you do not want to waste the exemption.

Now that the estate exemption has risen to $2 million per spouse this year, the cost of wasting it in the case of the first spouse to die is an incredible $920,000! That is the calculation of estate tax on a $4 million estate where only one $2 million exemption is available since the first spouse to die did not take appropriate estate planning steps. Even if the estate were only $2.5 million, your estate tax due would still be a hefty $230,000, not a small amount to "donate" to Uncle Sam. It could go to your heirs, with some simple planning.

The way that you take advantage of the estate tax exemption (also known as the credit shelter amount) is by setting up a credit shelter trust, also called a bypass trust. The two ways to set up such a trust are either a) through a living trust or b) through your will. Many of you have already taken such a step, but it's good to have your estate lawyer periodically review your documents. That's especially advisable since the amount of the exemption has risen to $2 million from $600,000 in only a few years.

One caveat, however: you need to be careful of the wording in the will or trust, depending upon your net worth. If a couple's assets, for example, total $2.1 million at the time of the first to die, and the will was set up to say that assets up to the amount of the federal estate exemption will be placed in a credit shelter trust, then all $2 million will indeed be placed into that trust. The result would be that a bypass trust would be set up using $2 million, with the children (in most cases) as the beneficiaries. That would leave only $100,000 for the surviving spouse to live on. Your estate lawyer needs to make sure appropriate wording is in the will or trust, so that enough is left outside the trust for the surviving spouse to live on.

So it pays to a) have the credit shelter trust set up and b) to check the wording with a competent attorney. Then you can rest easy that your heirs will get what they deserve, rather than your "relative" in Washington, Uncle Sam!