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Timing your death: What a difference a day makes

Imagine the Grim Reaper asks you to pick either Dec. 31, 2012, or Jan. 1, 2013, as the date of your death. Which would you choose?

While both death and taxes proverbially are inevitable, the date of your death can affect how much tax the government levies on your estate. Dying on New Year's Eve this year may leave your heirs with more money than your dying on New Year's Day next year will leave them.

BROOKE SALVINI
Viewpoint

That's because at the stroke of midnight on New Year's, the unified estate, gift and generation-skipping transfer tax is scheduled to change. For 2012, estates with assets of up to $5.12 million will not have to pay taxes. On anything over that amount, the federal government will charge a 35 percent tax. But in 2013, the exempt amount plunges to $1 million. The tax rate on the excess will range from 41 percent to 55 percent. (Congress, of course, could change the rules during the next nine months.)

I'm not in favor of anyone deliberately dying so his or her estate avoids paying taxes. I am, however, in favor of people taking all legitimate measures to minimize their estate taxes.

Most readers of this article probably do not have estates valued above $5.12 million, but many likely are worth more than $1 million. Regardless, good planning can ease or remove the tax burden on your estate.

Here are a few ways to ensure your heirs receive all you want them to have.

> **"You can't take it with you, but you can make sure your heirs are better off."**

• **Distribute part of your estate before you die**: You can give up to $13,000 to any individual during 2012 and not pay taxes on the distribution. If you are married, you and your spouse can give away $13,000 apiece to anyone. That means, for example, that the two of you could gift your daughter and her husband a combined $52,000 during 2012. If you give each person more than $13,000, the excess is taxed at 35 percent.

You may, however, invoke the unified credit rule to eliminate that tax. The credit allows you to give up to $5 million to individuals during your life without paying tax on any of it. You and your spouse can therefore give away a combined $10 million tax free over the course of your lives. (The giver is the party responsible for the tax, not the recipient.)

• **Pay for your grandchildren's education**: You can fund a grandchild's college tuition, which will reduce your children's financial burden and help your grandchild get a good education without going into debt. To keep the money tax free, you must pay the tuition directly to the educational institution. Furthermore, it cannot cover living expenses or books and supplies.

Nevertheless, the educational expense exclusion is separate from the gift tax exclusion discussed above. So you can give a grandchild up to $13,000 for room and board and other costs each year.

• **Pick up medical charges**. If a potential heir is hospitalized, needs expensive surgery, or requires physical rehabilitation, you can directly pay for the services. The unified credit rule does not come into play as long as you write the check to the hospital, not the patient.

• **Purchase life insurance**. Life insurance may or may not be considered part of your estate depending on ownership and beneficiaries. If you own the policy and have control over it (e.g., you can borrow on it or change beneficiaries), the policy's death benefit becomes part of your estate, unless the beneficiary is your spouse. If you establish an irrevocable life insurance trust as the policy owner, however, the death benefit does not pass through your estate. Incidentally, the beneficiaries do not pay income tax on the amount they receive.

Even if Congress extends the current estate tax exclusion to 2013 or beyond—or provides different rules for succeeding years—you would be wise to review your potential estate tax liabilities yearly. The stocks, bonds, business investments, personal property and the other assets you accumulate over a lifetime can result in a substantial estate. A financial planner such as a certified public accountant can help you find ways to conserve your assets and reduce the amount the government can claim upon your demise.

You can't take it with you, but you can make sure your heirs are better off.

• Brooke Salvini, CPA/PFS, CFP, is the owner of Salvini Financial Planning in Avila Beach and a member of the California Society of CPAs. Contact her at (805) 543-6622.