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QUALIFIED PERSONAL RESIDENCE TRUSTS: ESTATE TAXES AND YOUR HOME

Guy S. Emerich
June, 2007



Many clients would like to remove the value of their Florida residence from their estate for federal estate purposes. With the maximum current federal estate tax rate at 45% it is easy to understand!

One method is the creation of an irrevocable trust known as a Qualified Personal Residence Trust (QPRT). The trust is created for a term of years which the maker of the trust (settlor) must survive in order to gain a tax benefit.

When a person transfers title to this trust a gift occurs of the current fair market value of the residence. However, the Internal Revenue Code allows the settlor to subtract from the gift, for gift tax purposes, the actuarial value of his right to live there for the term of years that was selected.

For example, assume Mr. Jones is age 70 and in very good health. He owns a house valued at \$700,000. He creates a QPRT with a term for 15 years. (He could have picked any number of years.) In valuing the gift and preparing the gift tax return, the accountant subtracts from the \$700,000 the amount of \$562,366 which is the actuarial value of Mr. Jones' right to live in the home for 15 years based on the May 2007 federal midterm interest rate. The gift that is reported to the IRS is only \$137,634. Assuming Mr. Jones has never used his one million dollar lifetime gift exemption he does not have to write a check to the IRS.

If the house appreciates at 4% per year, then at the end of 15 years the house is worth \$1,260,660. Title then passes to the children or a trust for the children, grandchildren, or whomever Mr. Jones wants to get the home.



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Assuming Mr. Jones survives the 15 year term and further assuming he is in the 45% estate tax bracket, he has saved his heirs over \$505,000 in federal estate taxes! Even if Mr. Jones had selected a 10 year term instead of 15 years he still would have saved his family over \$345,000 in federal estate taxes. If he wants to continue to live in the home he can do so through a lease arrangement. He is then obligated to pay his beneficiary of the QPRT fair market rent. However, it is one more way to move assets from one generation to another instead of paying federal estate taxes. The lease can be arranged in such a way so as to not lose the benefit of the Florida homestead exemption and therefore the Save Our Homes Cap.

This is a great way to save federal estate taxes and still enjoy the use of your beautiful Florida homestead.

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