



Live in your home and give it away, too A QPRT can help you meet your estate planning objectives

A qualified personal residence trust (QPRT) provides a unique opportunity for you to make a significant gift to your heirs without having to divest yourself of any of your investment assets. While not for everyone, it may be the perfect way for you to meet your estate planning objectives.

QPRT inner workings

A QPRT may be ideal if your estate (or your and your spouse's estate) is large enough that you're likely to face estate tax liability at death. The trust allows you to gift your home, which isn't currently generating any income for you, to your children or other heirs, but you may continue to live in it.

By removing the property's future appreciation from your estate, you're leveraging the gift today so that, at your death, your children (or other beneficiaries) will inherit a greater amount at a lower estate tax cost than if you had not transferred the home to the QPRT.

Jerry, Ruth and a QPRT

Let's suppose Jerry, 80, and Ruth, 75, own a home worth \$2 million, and that the couple has a combined estate of nearly \$10 million. They're interested in a QPRT because their estate isn't terribly liquid and they want to retain the liquidity they have to ensure they can live comfortably for the rest of their lives. Also, they want to be sure there will be enough ready money at the survivor's death to pay the estate tax.

Even though it's possible the children will not choose to retain the property after their parents are gone, the family is hoping they'll be able to keep the home. Jerry and Ruth believe a QPRT will give them the best chance to do that.

In addition, the couple likes the fact that they can decide how long the trust will last. The term of the trust is part of the gift calculation of the QPRT, which also uses the IRS Section 7520 rate and the age of the person(s) transferring the property to the trust to determine the value of the gift.

Jerry and Ruth have decided that Jerry will transfer his ownership interest in the home to Ruth, and she alone will make the gift to the QPRT. Because they're making the gift at a time when the Sec. 7520 rate is 6%, they determine that a seven-year term is appropriate. The value of the gift, therefore, based on the calculation using those factors, is slightly more than \$900,000 (rather than the full \$2 million fair market value of the home).

If Jerry and Ruth keep their home and it appreciates at an average of 8% per year, the house will be worth more than \$3.4 million at the end of the seven years. Supposing the survivor of Jerry and Ruth dies at that time, and presuming the estate tax rate is 45%, estate tax in excess of \$1.5 million is attributable to the value of the home.

QPRT risks

A QPRT is not without risk. First, there's the risk that Ruth will not survive the term. If she doesn't, the QPRT will have been for naught because the transaction will be disregarded: The house will be included in Ruth's estate. In their case, though, Jerry and Ruth decide that a seven-year term for Ruth is an acceptable risk to take because Ruth is in good health and both of her parents lived into their late 80s.

The other end of the risk spectrum is that Ruth will live far beyond the QPRT's term. After the QPRT terminates, Ruth no longer will own the home. Instead, the children will own it, either outright or in trust, and Ruth will be obligated to pay rent to live in "her" house. While the likelihood is that cash flow won't be an issue, and that Ruth will be able to afford to stay in the house, there is an unease related to the possibility that she'll be forced to leave the home.

Another consideration is that Ruth may not want to live in the house alone after Jerry's death. This is a genuine concern, but, again, they reason that, if that happens, Ruth will have sufficient cash flow – and other assets – to continue to live comfortably.

Jerry and Ruth also realize they're forgoing the \$500,000 capital gain exclusion that would be available to them if they were to sell their home. But, they reason, they aren't planning to sell, so this isn't a concern. However, they also realize the lost step-up in basis could translate to significant extra income tax being paid by their children should they decide to sell the home after Jerry and Ruth die. They've weighed this, however, against the potential estate tax savings, and decide, again, that they're willing to take the risk.

Weigh the benefits

A QPRT can lead to significant tax benefits, but carefully consider all of the potential positives and negatives before deciding that you want to move forward. You may find that a QPRT is the right way for you to make a significant gift to your family without having to deplete your investment assets.

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