



ESTATE PLANNING CAN BE TAXING

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Last month, in *Avoid Estate Planning Mistakes*, we discussed the nitty-gritty details that must be addressed for your estate plan to work. We outlined the importance of ensuring that your documents are current; choosing appropriate trustees, executors and/or guardians; how to hold title to assets; funding trusts; communicating your estate desires to your family; etc. Most financially successful people have done some type of estate planning, but all too often, they have engaged in what we call “piecemeal planning.”

They have implemented a piece here and a piece there in hopes that all these pieces will fit neatly together when all is said and done. That rarely happens. Every year in this country, billions of dollars are lost to unnecessary estate taxes caused by “piecemeal planning.” So let’s look at several tax-related issues to consider when designing your master estate plan.

Death and taxes may be inevitable,
but they shouldn't be related.
J.C. Watts Jr.

Using the Full Exemption Equivalent Credit

The "exemption equivalent credit" simply means you can pass up to \$2 million to whomever you want without paying any estate tax. One of the biggest mistakes married people make is leaving all their possessions outright to their spouse. When this is done, neither spouse takes full advantage of his or her exemption equivalent credit. This can result in unnecessary estate taxes at the second death.

If your estate is more than \$2 million, you might consider a "credit shelter trust," or "B Trust" for each spouse, to maximize the value of the combined exemptions. Income can be paid out to the surviving spouse from the credit shelter trust and principal can also be tapped in order to support the lifestyle of the surviving spouse. Under current law, this technique allows a married couple to pass up to \$4 million completely free of estate tax.

Equalize Spousal Estates

Often, one spouse ends up with more of the financial goodies in his or her name. For instance, the primary bread-winner may accumulate a much larger retirement account than the other spouse. Assets over \$2 million and under \$4 million pass estate-tax-free only if the couple equalizes the estate to properly utilize their A/B trust.

It is crucial to be smart about titling assets at the inception of your estate plan. But it is equally important to continually monitor asset values over time. You may have a masterfully written plan, but if you become complacent about knowing the value of what

you own and how that impacts your estate strategy, over-taxation could be the unintended result.

Using an Irrevocable Life Insurance Trust

Another common way to manage estate taxes (especially for estates exceeding \$4 million) is to hold life insurance policies in an irrevocable life insurance trust (ILIT). The trustee of the ILIT is made the owner and beneficiary of your life insurance. As long as you live three years after transferring the policies to the ILIT trustee, all insurance death benefits pass free of both estate and income taxes.

Bottom Line

Estate planning is just one piece of the financial planning process – albeit a very important one. The most effective approach is starting with what really matters to you, your loved ones, and the legacy you want to leave. Once you have clarity about your unique goals and objectives, you and your trusted advisor can craft – and implement - a master plan that addresses all of your financial, tax, investment, insurance, charitable, and legal objectives.

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