QUALIFIED PERSONAL RESIDENCE TRUSTS:
Your Home Can Be Your Legacy to Your Loved Ones

HOW DO YOU FEEL ABOUT YOUR HOME?

Is it a sense of…

- Pride? For months you were a "weekend warrior," spending every weekend painstakingly and lovingly renovating your home.

- Joy? You look forward all year to the two weeks all of your children and grandchildren get together to spend vacation time in the big, beautiful family summer cottage on the beach.

- Achievement? When your escrow closed on your stunningly majestic home, you felt a surge of accomplishment, and that all of your hard work had finally begun to pay off.

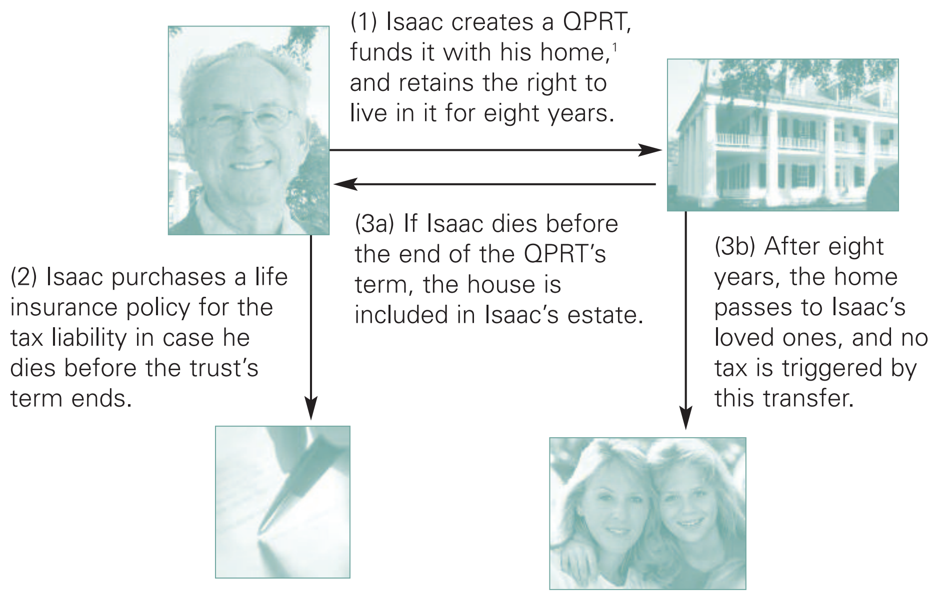
While you have been enjoying your dream home, have you thought about ways to ensure that your loved ones can continue to take pleasure in it long after you are gone? There is a way to preserve your home for the benefit of your family for generations to come, and at a reduced tax cost. This strategy employs a type of trust called a QPRT, or "qualified personal residence trust." A QPRT (pronounced "cue-pert") is a type of irrevocable trust, funded with your home. You would keep the right to live there for a period of time and, after that, its ownership passes to your loved ones. Because you retain the right to live there, its gift value is less than its fair market value. Consequently, the gift tax due would be much lower than giving the house to your loved ones outright.

You must outlive the trust's term to receive the benefits of the discounted gift. If you pass away before the QPRT's termination date, the value of the trust's assets—the home—is included in your estate again and the trust is ignored. To safeguard against this possible outcome, you can purchase a life insurance policy equal to the amount of the estate tax increase if the home ends up being included in your estate again.

HOW DOES A QPRT WORK?

Meet Isaac.

Isaac is a 74-year-old widower. He owns a beautiful turn-of-the-century Colonial mansion in the rustic Berkshires area of Massachusetts. Every year, his three sons and their families gather at Isaac's home for two weeks of idyllic vacation time. Isaac wants to ensure that his family can enjoy the benefits of his home as a family vacation home long after he has passed away.



[1] Isaac's gift tax liability is discounted due to his retention of the right to live in the home for a period of years. The gift to his remainder beneficiaries is a gift of a future interest, so it will not qualify for the gift tax annual exclusion. However, Isaac can allocate all or a portion of his lifetime gift exemption amount to the value of the gift.

At an Internal Revenue Code Section 7520-rate of 5.6%,[2] and assuming his home's value is $1.5 million, the value of Isaac's retained interest is about $865,000, assuming a QPRT with an eight-year term. As a result, at the end of eight years and with an appreciation rate of 4%, Isaac would have passed an asset worth more than $2 million at a gift tax value of approximately $635,000 to his loved ones. That's more than $1.3 million of property transferred gift tax–free!

At the end of the QPRT's term:

- Isaac has passed on a valuable asset at a discounted gift tax cost.
- When Isaac passes away, the value of the home is excluded from his estate.
- All appreciation on the home is now in the hands of Isaac's loved ones, rather than being subject to estate tax in his estate.
- If Isaac wants to continue to live in the home after the termination of the trust, he can do so by paying rent to his loved ones at a fair market value rent. The rental payments remove additional assets from Isaac's gross estate without being subject to gift or estate taxes. Isaac's loved ones would recognize the rental payments as income when received.
- Although Isaac's loved ones receive a proportional carryover basis in the property, no capital gains tax would be due until his loved ones decide to sell the property.
- Isaac has preserved his family's memories and connection with a long-standing tradition that may now continue indefinitely.

[2] *The IRC § 7520 rate is the rate used by the IRS to measure a life expectancy.*

WHAT ARE ISAAC'S OTHER OPTIONS TO PRESERVE HIS HOME?

Should Isaac not be comfortable with giving away the ownership and title of his home through the use of a QPRT, he may instead want to consider using life insurance to cover any transfer costs of the property at the time of his death. With extensive property appreciation in many parts of the country over the last few years, Isaac may not have realized that the value of his home, when combined with his other assets, may create an estate tax liability at his death.

Life insurance, properly structured to keep its death benefit excluded from Isaac's gross estate, could offer liquidity at his death to pay estate taxes, any remaining mortgage on the property, or to equalize the estate should he intend the property to pass on to one heir rather than to benefit all of his loved ones.

Whether through the use of a QPRT or life insurance, you, just like Isaac, have several options to preserve your family home for your loved ones. The key is to take planning steps now to maximize your family legacy.

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