How to Prepare for the Return of the Estate Tax

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A recent article in Forbes magazine rightly noted that, with the prospect of only a $1 million per estate exemption looming as a possibility for 2011, many more Americans need to have an estate plan in place, especially if they have children.

The report gave some good information on simple steps you can take now to protect your assets for your heirs, including:

Don't die owning life insurance. If you die leaving life insurance to someone who is not your spouse or a charity, money from that policy will be subject to estate tax. Instead, put the policy in the name of the recipient and gift them enough every year to pay the premiums.

Put assets in each spouse's name. Dividing assets (except retirement accounts) and putting some in each spouse's name allows a couple to properly fund a bypass trust that will provide more benefits to the surviving spouse and children.

Maximize your gifts. An individual can give up to $13,000 every year to as many beneficiaries as he or she likes; a couple can gift up to $26,000 jointly to anyone every year. But before you give, make sure you have enough for your own retirement.

Pay medical expenses and tuition. You can pay tuition and healthcare expenses for anyone you want as long as you pay the providers directly. Such payments are not calculated toward your $13,000 annual gift limit, either.

Fund a college savings plan. You can fund a Section 529 college savings plan and earnings are exempt from federal and state income taxes as long as the money is used to pay tuition or certain college expenses.

Roth IRA conversion. Converting a traditional IRA or 401(k) to a Roth IRA will allow you to avoid having to take the annual minimum distributions once you hit the age of 70 ½, which can leave more for your beneficiaries. Plus, once you pay any income taxes on pretax contributions or earnings, all future growth is tax-free.