www.lawyersusaonline.com
Lawyers USA

Practice makes perfect. Sub
SIGN
FREE
E-ma

Wednesday, July 12, 2006

Lawy

From the January 05, 2004 Lawyers USA.

Order a REPRINT of this Story

Guest Article

Happy New Year: It's Time To Revisit Your Clients' Estate Plans

By Jeffrey A. Baskies

This new year marks an important milestone in estate planning. Effective Jan. 1, the federal estate tax exemption has increased 50 percent from $1 million to $1.5 million.

This change has far-reaching applications and importance. While the $500,000 increase is just one step in the phased-in increase of the exemption scheduled through 2010 under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), for many clients it marks an important opportunity to revisit their estate plans.

ADVERTISEMENT

Get client newsletters tailored to your practice areas!

Click here for more information.

1. For clients with estates under the exemption

For clients of moderate wealth - let's define that as individuals with less than $1.5 million and couples with estates of $3 million or less - this change may be the difference between having a taxable estate and not having one.

For individual clients, this is a time to review their plans to ensure they are happy with their distributions.

For example, a client may have planned to make charitable gifts so as to minimize estate taxes on death, but if the estate is no longer subject to estate tax, the client's intentions may no longer be apt. In this example, there may be no tax to consider. That doesn't mean the client's plan needs to change, but as the client's planner it behooves you to meet the client and discuss the changed circumstances so the client can make an informed decision.

For married clients, 2004 is a time review estate plans to be sure the surviving spouse has enough wealth after the first death. Many estate plans crafted in the past 20-plus years provide a formula "credit shelter/marital deduction" formula.

The formula generally calls for the exemption amount (now $1.5 million) to flow to the credit shelter trust and the rest (residue) to pass to the spouse (outright or in trust). Such formulas are important to maximize the federal estate tax exemptions of both spouses. But the maximum passing to the credit shelter trust may no longer be the client's preference.

For example, a married couple with less than $1.5 million in assets who created an estate plan prior to EGTTRA would likely have had such a plan. The credit shelter trust assets could benefit the spouse (and often the descendants too) during the survivor's life but then passes tax-free on the survivor's death (as it was protected by the estate tax exemption of the first spouse to die). But now, they may not need a credit shelter trust at all. Or, a surviving spouse may not be happy to find that the survivor's entire inheritance is tied up in a trust (where the survivor may or may not even be a trustee). In some cases, the credit shelter amount went to a trust or went outright and didn't benefit the survivor at all. When the exemption amount was "only" $600,000 that may have been acceptable to the clients, but now the exemption amount may wind up being the entire estate. And that may not be acceptable at all.

Thus, it is important that we contact those of our clients who have a credit shelter trust funded by a formula clause. For clients who have such formula clauses, we need to discuss if the portion of their estate which will now be allocated to such trust (up to $1.5 million, as opposed to perhaps $600,000 - their intention when the plan was created) is consistent with their present wishes.

This is also a time to reconsider the need for life insurance trusts or other irrevocable arrangement(s) that may have been viable before the increased exemption. For example, a married couple with $2.5 million in assets may have been well advised to consider a second-to-die policy (in an irrevocable life insurance trust, or "ILIT") under the pre-EGTTRA rules and the old $600,000 exemption. But now the estate can avoid taxes with proper credit shelter planning and there may be no tax need at all to continue paying premiums on that second-to-die policy. Now, the clients may feel the "investment" in the policy justifies continuing it, but again, it is our jobs as planners to make sure we inform our clients of the changes in the law so they can make their own informed decisions - rather than "blissfully" paying for policies they may no longer want.

Another important issue for clients of moderate wealth is planning for IRAs and pension fund assets. While the stock market bubble burst in 2000, there are still many clients with substantial assets in retirement plans. These assets still pose substantial problems for those planning to maximize their estate tax exemptions. The increased exemption may allow for easier planning by shifting non-retirement assets around. Moreover, if clients in this moderate wealth category previously designated a credit shelter trust to receive retirement assets, that may no longer be necessary. So retirement plan beneficiary designations should also be reexamined in 2004.

2. For clients with estates larger than the exemption

While the increased exemption will clearly provide relief by potentially eliminating the federal estate tax payable by clients of moderate wealth, it also offers opportunities for wealthier clients (let's consider these to be individuals with estates over $1.5 million and couples with estates over $3 million).

For clients with large estates, the increased exemption will likely have less impact on their basic plan - their wills or revocable trusts will still need credit shelter trust planning. While the increased exemption will certainly allow more assets to pass to their descendants tax-free, if their estates are large enough, they still face substantial estate tax issues. For these clients, the increased exemption may be more significant for other leveraging opportunities it provides.

What is particularly problematic about this change is the de-coupling of the estate and gift tax exemptions. For the first time in many of our careers, those exemptions are no longer the same. The federal gift tax exemption is stuck at $1 million while the estate tax exemption is rising (to $1.5 million this year). That de-coupling poses planning issues worthy of extra attention.

First, many of our wealthiest clients have made lifetime gifts that used up their estate tax exemption amounts. Pre-EGTTRA that may have meant gifts up to $1.2 million for a couple. But they may not have used the $800,000 increase that has since been created under EGTTRA. Our wealthy clients will likely want to take advantage of that increased exemption, and we should alert them of the opportunity.

Second, our wealthiest clients should still consider the advanced techniques available to them. The increased estate tax exemption makes discounting vehicles (family limited partnerships or limited liability companies) even more important. Also, our wealthiest clients may wish to make gifts via Chapter 14 trusts (Walton GRATs are very popular opportunities to shift wealth without incurring additional gift tax), or clients with some gift tax exemption left may prefer to make use of taxable GRATs - which may allow clients to significantly leverage their gift tax exemptions. Either way, the clients will expect to be alerted to these new opportunities and will appreciate hearing it from you - their tax advisor - first.

Moreover, these clients may be interested in some of the most interesting ways to control their future gifts/bequests. They may want to establish trusts for their gifts (or for their estates to manage the increased estate tax exemption amount) to offer asset protection for their beneficiaries. They may wish to utilize an extended rule against perpetuities to create trusts that last for many generations. Moreover, they may wish to use charitable vehicles to further leverage their exemptions (for example a charitable lead trust may be a great way to use some of the increased exemption).

Wealthy clients should also take advantage of this time to reconsider their irrevocable arrangements and retirement plan beneficiary designations (as described above). While they are less likely to be impacted by the law change, they may still benefit from a current review.

Conclusion

The bottom line for estate planners is the substantial change in the federal estate tax exemption effective on Jan. 1 should be a reason to contact all of our clients. Our wealthiest clients will now have a chance to make further tax-free transfers that will ultimately help minimize transfer taxes by removing assets from their taxable estates. While our more modestly wealthy clients may need to revise their estate plans entirely. Take advantage of the changes taking effect to contact your clients.

Jeffrey A. Baskies, Esq., who practiced estate planning in Florida for many years, is currently the CEO of Lawyers Weekly Inc. in Boston. Board certified as a specialist in wills, estates and trusts law by the Florida Bar, his column runs regularly in Lawyers Weekly USA, the national newspaper for small law firms. If you have questions or issues relating to estate planning, please feel free to e-mail Jeff at jbaskies@lawyersweekly.com. All questions are encouraged.

© 2004 Lawyers Weekly Inc., All Rights Reserved.

Order a REPRINT of this Story

LawyersUSA Try 6 Weeks Free Newspaper

User Agreement For Subscriber-Only Online Benefits | Help | Our Privacy Policy
Send any questions or comments to comments@lawyersweekly.com

Subscriber Services: 1-800-451-9998 **Technical Support**: 1-800-444-5297 ext. 8156

© Copyright 2006 Lawyers Weekly, Inc. All Rights Reserved

Lawyers Weekly does not use spyware; however, we link to a number of other sites and do not take responsibility for any spyware they

This site is best viewed with Internet Explorer 6 (click here to download) or Netscape 7 or higher (click here to download)

208.49.101.98/5.93