



# The Wealth Advisor

## Estate Planning You Can...and Should ...Do In 2010

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With the current economy and uncertainty about the federal estate tax, many people are finding themselves sitting on the fence, wondering if they should do any estate planning now, or if they should wait. You may be surprised to know that there are many non-tax reasons to plan your estate that have nothing to do with the economy or estate taxes. And if your estate may be subject to estate taxes in the future, this year can be a perfect time for many people to plan, specifically because of historically low interest rates and changes that have been proposed by the IRS and Congress.

Let's look first at planning needs that are not related to the economy or to the estate tax.

### Disability Planning

It's a fact that most of us will need some kind of assistance with our daily living activities for at least some time before we die. This kind of care can be provided in your home, in an assisted living facility, or in a nursing home. All can become very expensive.

Home health care can easily run over \$20,000 per year. That's at \$16 per hour, for just 25 hours a week.

Depending on the skill required, number of hours needed and where you live, it can cost considerably more. Assisted living facilities can cost more than \$25,000 per year; the more services you need, the higher the cost. Nursing home facilities, with round-the-clock care, are easily \$50,000 or more a year.

Take a look at these statistics for Americans age 65 and older:

- 43% will need nursing home care;
- 25% will spend more than a year in a nursing home;
- 9% will spend more than five years in a nursing home; and
- the average stay in a nursing home is more than 2.5 years.

From [Edward Marin](#)

**Meyers, Rodbell & Rosenbaum, PA**

1445 Research  
Boulevard, Suite 301  
Rockville, MD 20850  
301-738-7061

EDWARD S. MARIN,  
J.D., C.P.A., LLM-Tax  
practices in the areas  
of Trusts and Estates,  
Estate, Gift and  
Income Tax Planning,  
Probate, Trust  
Administration,  
Business Succession Planning and  
Charitable Planning. In addition to being a  
practicing attorney, Ed is also a Certified  
Public Accountant.



**Planning Tip:** Most insurance plans and Medicare do not currently cover long-term care. That means the cost will need to be paid from your assets. Consider purchasing a long-term care insurance policy to protect your assets.

Besides the cost of long-term care, you may also be concerned about who will provide the care you need and where you will receive it. You may prefer to stay in your home for as long as possible, or you may enjoy the companionship and social aspects of an assisted living facility. However, incapacity can deprive you of the ability to make your desires known and implemented.

**Planning Tip:** Your trust can include disability provisions that will make sure your desires are clearly expressed and carried out. It's best to take care of this now, while you are able to communicate your wishes.

### **Special Needs Planning**

Here are some more eye-opening statistics. These are from the U.S. Census Bureau report in 2000. (It will be interesting to compare these when the latest Census reports are available.)

- 51.2 million Americans reported having a disability;
- 13-16% of U.S. families had a child with special needs;
- 15 out of every 1,000 children born in the U.S. had an Autism disorder;
- Between 1 and 1.5 million American had an Autism disorder.

Thanks to medical care advances in recent years, many with special needs now outlive their parents and/or caregivers. Planning that does not include specific provisions for the special needs person can have disastrous consequences, including the loss of valuable government benefits.

**Planning Tip:** A Special Needs Trust is a critical component of planning for families with a special needs person. This trust can provide the ongoing support the special needs person requires without jeopardizing government benefits.

**Planning Tip:** Insurance on the life of a parent, grandparent or other relative can provide the trust funds necessary to pay for care and extras that are not provided by government benefits.

### **Inheritance Protection Planning**

Protecting an inheritance from predators, creditors, divorce and irresponsible spending is a major concern for many parents and grandparents today. Many feel that their children and grandchildren lack strong financial skills, and difficult economic times can make inheritances more vulnerable to creditor claims and/or maintaining a lifestyle beyond the beneficiary's means.

Difficult economic times also increase the likelihood of divorce, which is already at a 50% rate. Most people do not want to see their hard-earned money ending up in the hands of a former daughter- or son-in-law.

**Planning Tip:** Your trust can include provisions to protect inheritances from divorce, creditors and from the beneficiaries themselves.

### **Blended Family Planning**

More divorce leads to more marriages and blended families - his, hers and, sometimes, theirs. Each parent needs to make sure his/her children are protected, especially if you will also leave a surviving spouse. Not doing so can cause your children to be unintentionally disinherited or, at the very least, create a messy probate battle.

**Planning Tip:** Your trust can include provisions that will allow you to provide for your surviving spouse and make sure your children (and grandchildren) receive the inheritance you want them to have.

### **Planning for Estate Taxes**

Yes, you do need to plan for estate taxes now, even though we currently do not have a federal estate tax in 2010. Here's why:

*Reason One.* Most states now have their own inheritance/death tax, so even though your estate may not have to pay a federal tax, it may have to pay a state tax. This is true whether you die in 2010 (when there currently is no federal estate tax), or if your estate is small enough that it will be exempt from the federal tax. Depending on where you live, an estate as small as \$388,000 could be subject to a state death tax.

**Planning Tip:** Don't assume your estate will not have to pay estate taxes. Now is a good time to find out about your state's death/inheritance tax and plan for it.

*Reason Two.* Chances for permanent repeal of the federal estate tax are essentially zero. With all its spending programs, Congress is going to want/need every tax dollar it can get its hands on. The only questions are when will Congress act and what will it do. The more time that passes this year, the less likely it is that Congress will change anything for 2010. That's because both parties will probably make the estate tax an issue for the mid-term elections in November. If Congress does nothing this year, the estate tax will return in 2011 with a \$1 Million exemption and a 55% tax rate. Compare this to the 2009 estate tax that had a \$3.5 Million exemption and a 45% tax rate. There is no question that more people will be paying more in estate taxes.

**Planning Tip:** Don't wait until 2011 to plan. You could become physically or mentally incapacitated before then due to an illness, injury or accident. Plan now while you are able to do so.

*Reason Three.* Congress will almost certainly eliminate several wealth transfer techniques that will affect your ability to transfer assets to your beneficiaries at discounted values. Combine this with interest rates that are at an all-time low and depressed property and investment values, and you have an exceptional planning opportunity that can save substantial amounts in estate taxes and provide more for your loved ones.

For example, let's say you wanted to use a Family Limited Partnership (FLP) or a Family Limited Liability Company (FLLC) to, among other things, transfer a family business, farm, real estate or stocks to your children. In exchange for transferring the asset to the FLP or FLLC, you will receive ownership interests. You will have a fiduciary interest to other owners, but you can keep control as the general partner (FLP) or manager (FLLC). You can also give ownership interests to your children, which removes value from your taxable estate. And since these interests cannot be easily sold or transferred their value is often *discounted*. In other words, since most people would not pay full price for an asset they could not sell or transfer, its value is worth less than the value of the underlying assets. This lets you transfer the underlying assets to your children at reduced value without losing control.

### **Other Planning Options**

There are other planning options that let you transfer assets at discounted values and benefit from historically low interest rates. Here are two:

- *Grantor Retained Annuity Trust (GRAT)*: Lets you transfer an income-producing asset (stock, real estate, business) to a trust for a set number of years, removing it from your estate, while you receive the income it produces. When the trust term ends, the asset will go to the beneficiaries of the trust. Because they will not receive it until then, the value of the gift is reduced (discounted). If you die before the trust term ends, some or all of the asset may be included in your estate for estate tax purposes.
- *Charitable Lead Trust (CLT)*: This charitable trust lets you transfer an asset into a trust for a set number of years or until you die. During this time, the charity or charities you select will receive the first or "lead" right to receive a stream of equal payments from the trust. At the end of the trust term, whatever is left in the trust (the remainder) will go to the beneficiaries of the trust, typically your children or grandchildren. Because the gift to the beneficiaries is delayed, the value is substantially reduced, resulting in little or no estate tax on the asset. CLTs are particularly suited for hard-to-value assets (such as real estate or family limited liability company interests) and assets which are expected to grow rapidly in value.

**Planning Tip:** While strategies like these have been used effectively for years to reduce estate taxes, it is no secret that the IRS is not fond of having to accept discounted values. With Congress looking for every possible way to increase revenue, many of these strategies could soon be eliminated. For example, a current proposal in Congress would eliminate GRATs with a term of less than 10 years, making it more likely that the GRAT assets would end up back in your estate. 2010 is an exceptional year to make good use of these strategies, while we still have them.

**Planning Tip:** *Making gifts now can save estate taxes later.*

Currently, each year you can give up to \$13,000 tax-free to as many individuals as you like; you can double that amount if your spouse joins you. For example, if you have three children

and six grandchildren, you can give them a total of \$117,000 (\$234,000 if your spouse joins you) each year. If you give more than this, it will be applied to your \$1 Million lifetime gift tax exclusion (\$2 Million if your spouse joins you). After that has been exhausted, you will pay a gift tax, but it is currently 35%. That's a lot less than estate taxes, which have historically been 45-55%.

Plus, any appreciation on gifts you make now is also out of your estate. Say you transfer \$1 Million to your children today. Assuming these assets grow at 10%, in ten years they will be worth \$1,930,690. If you wait and give the \$1 Million to your children when you die, and we assume the estate tax exemption is \$1 Million, the \$1,930,690 will be subject to federal estate tax of at least \$418,810, leaving just \$1,511,879 for your children.

**Planning Tip:** *Using a Grantor Trust can provide even more for your children.*

A Grantor Trust is a separate irrevocable trust that you can establish for estate planning purposes. The rules are different, which can be used to your advantage. For example, without getting too technical, the IRS defines a Grantor Trust one way for income taxes and another way for estate and gift taxes; in other words, the rules don't match. By using this long-standing "wrinkle," in the tax code, transfers of assets by gifts and sales to irrevocable trusts can be "supercharged," letting you transfer even more to your children estate tax free. For example, if you used a Grantor Trust and paid the income tax, the same \$1 Million gift would grow to \$2,592,742, which is \$663,052 more than if the gift were made directly to your children and they paid the tax.

## Conclusion

Take advantage of the rare planning opportunities that exist now, that can save substantial amounts in estate taxes and provide more for your loved ones. For more information about estate planning in 2010, please contact our office.

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Meyers, Rodbell & Rosenbaum, PA 1445 Research Boulevard, Suite 301 Rockville, MD 20850 [Website](#)

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