ESTATE PLANNING

Ideas to Help You Plan for Your Future

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FAMILY LIMITED PARTNERSHIP STILL HOT...

A VERY VIABLE ESTATE PLANNING STRATEGY

The Family Limited Partnership (FLP) remains the hottest estate planning vehicle. Aside from valuation discounts to avoid estate taxes, the FLP has multiple benefits :

$ Retains parent's control of family wealth

$ Avoids descendants dissipating family wealth

$ Protects family wealth against creditors of descendants

$ Avoids family wealth going to in-laws in the event of divorce.

The biggest attribute of FLPs is their valuation discounts in regard to estate taxes. Assume you are in a 55% estate tax bracket and you put $1 million in assets in an FLP and give interests in that FLP to your descendants. Say the value of those gifted interests are discounted 40% due to lack of marketability. That could save the family $220,000 in estate and gift taxes (55% of 40% of $1 million)!

The IRS has not been happy about FLPs. The IRS has issued Technical Advice Memoranda (TAM) which purport to disregard the valuation discounts. Usually, the IRS position in these TAMs is that the FLP lacks business purpose and that it is merely a sham device to transfer family wealth without paying estate tax. The TAMs also challenge the valuation discounts on some technical statutory grounds.

Interestingly, when in court the IRS has not been very successful in challenging FLPs. In several court cases where the IRS argued the points made in the TAMs, the IRS has folded when challenged by the taxpayer, or the court has ruled in favor of the taxpayer. In the only reported decision I have seen where the taxpayer lost, the taxpayer failed to respect the formalities of the FLP. He controlled the FLP and used it like his personal checkbook. Further, he did unbusiness-like things like putting his house in the FLP and continuing to live there rent-free.

To summarize, FLPs remain a very viable estate planning device. However, to make them work you must treat them as a business entity, and it is essential to obtain a high quality appraisal to substantiate valuation discounts.

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“DO YOU WANT TO BE A MILLIONAIRE?”

NO THANK YOU REGIS, JUST A COLLEGE GRADUATE WITHOUT A MILLION DOLLARS IN STUDENT LOANS

With the cost of college continuing to skyrocket, many parents cash in retirement plans, take out second mortgages or sell stocks in an effort to pay college bills. However, now there is a simple and tax friendly plan that can help save for children’s college expenses and at the same time aid grandparents in lessening their estate taxes.

Section 529, a recent amendment to the Internal Revenue Code, allows donors to make tax-free gifts to college savings plans for children or grandchildren. The donors retain control of the account and may even take back the money if they wish. The money in the account may be used to pay for tuition, fees, supplies, room and board, books, and equipment required for enrollment at an undergraduate, graduate, or occupational school. With many states’ plans, the account funds may be used for any accredited college in the US or abroad! There are no restrictions on when an account may be opened. However, it must be opened for at least 36 months before funds can be withdrawn without penalty. In addition, there are several options to continue the account tax-free if the beneficiary of the account decided not to go to, or finish, college.

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These state-run savings plans are beneficial in not only saving for college but they also can provide large estate-tax breaks. Here’s why: affluent taxpayers — those with net worth in excess of $1 million — may leave taxable estates at death subject to rates as high as 55%. The easiest way for folks to decrease their estate net worth is by making annual gifts to each child, or grandchild. Each contributor to a Section 529 savings plan may contribute up to $50,000 all at once for the beneficiary and elect to amortize their gift-contribution over five years. When the donor makes this gift it is a tax-free, completed gift. The amount earns income and compounds tax-free like an IRA. When the child gets the money for college, he pays income tax on the fund’s earnings, but not on the original gift. As long as the original donor remains the account’s owner he or she may change the beneficiary or even take the money back!

The college savings programs vary from state to state. Certain states, such as New York and Maine, have hired professional fund managers such as Merrill Lynch, TIAA-CREF, Fidelity, and Vanguard among others. These professional advisors have invested account assets in traditional stocks, bonds, mutual funds and other balanced investment alternatives. Other states, such as North Carolina, have invested fund monies in state and local bonds. Several states, such as New York and Maine, allow non-residents to invest in their plans; an important fact for an investor looking for an aggressive investment strategy to consider. For more information on Section 529 state college savings programs visit the web site: www. savingforcollege.com.

"WHEN IN DOUBT DO NOTHING"

Unfortunately, that advice does not fit in regard to estate planning. I often meet with clients and offer them a menu of estate planning options; the numerous choices appear overwhelming, and the clients can't make up their minds. So, nothing gets done. When I work with clients who have a number of estate planning choices available to them, I generally make a list of priorities and suggest that we gradually peck away at the list. For instance, if you are considering Wills, Powers of Attorney, Health Care Declarations, a life insurance trust, and a charitable remainder trust, you should execute the Wills, Powers of Attorney and Health Care Declarations first. Next, before you get any older and the insurance becomes more expensive, create the life insurance trust and purchase the life insurance. Then address the charitable remainder trust.

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Your Wills can be changed at any time."

Guardians for Children

A recent article suggested that the single biggest thing which keeps people from executing their estate plan is the inability to choose a guardian for their minor children. A parent is certainly not doing his or her children any favor by not making a decision about a guardian. If both parents were to pass away without having named a guardian, someone in one of the families would hopefully step forward. But would that be who the parents would have chosen? Is that volunteer really suited to raise the children? Perhaps someone outside of the family would have been a better choice. Unfortunately, non-family members will not usually step forward and inject themselves into the mix. Further, a court, without guidance from the deceased parent's Wills, will not usually prefer a non-family member in a guardianship proceeding.

When our children were minors my wife and I wrestled with this very problem. We did not feel that family members had the parenting skills to raise our daughters. Over the years, we re-wrote our Wills two or three times to change the designated guardians for our children. It seemed that long airplane flights were often the catharsis for this exercise. But the point is that at least we did it. My recommendation to parents of small children is to get Wills in place as fast as possible, and designate guardians for your children. Your Wills can be changed at any time.

In choosing a guardian, consider not only love for your children and family relationships, but also who is physically and emotionally equipped to handle children. Grandparents may love their grandchildren very much, but may not be up to dealing with rambunctious children on a daily basis. Don't worry about hurting the feelings of relatives by naming non-family members. First of all, you won't be there to be the target of those hurt feelings. But more importantly, doing what is best for your children is much more important than some wounded feelings.

Powers of Attorney and Health Care Declarations

The inability to come to a decision about estate planning matters also impacts decisions with regard to living matters. I recommend to all of my clients for whom I do estate planning that in addition to Wills, they also have a Durable Power of Attorney and a document dealing with Health Care in case of incapacity. In some states the Health

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Care Declaration is called a Health Care Proxy, in others a Power of Attorney for Health Care, in others a Living Will — I will refer to them collectively as Health Care Declarations.

The Durable Power of Attorney designates someone who can handle business matters for you if you become incapacitated. It is called durable because it is not revoked if you become incompetent.

If you become unable to handle business affairs due to illness or incompetence and you do not have a Power of Attorney, it will be necessary for a court to appoint a Guardian for you. That proceeding is time-consuming and expensive. Further, the choice of the Guardian is taken out of your hands and put in the hands of a judge.

A Power of Attorney is an inexpensive and efficient way to protect yourself and your family in case you become incapacitated.

Similarly, a Health Care Declaration can save your family considerable anguish if you are seriously ill or injured. The Declaration will authorize someone you have chosen to make health care decisions on your behalf, including decisions with regard to life support if you are in a terminal condition.

If you do not have a Health Care Declaration a judge may end up making the decisions in regard to your health care. Most of my clients would prefer to be removed from life support if they are terminally ill and likely to pass away soon. However, a judge may not see it that way.

When you do see your attorney to plan for the future it is important to take some time to consider his or her suggestions, plans, and comments. But, don't take too much time. Repeatedly putting estate planning decisions on the back burner may simply lead to larger than expected dilemmas and problems in the future.

Next Issue: Wills vs. Living Trusts
Which is Better?