KOWALCZYK, DEERY, HILTON & BROADBENT, LLP

ESTATE PLANNING QUARTERLY

NEW ESTATE PLANNING TECHNIQUES FOR THE BABY BOOMERS -- LIFE INSURANCE TRUSTS ARE BACK AND BETTER THAN EVER!

With the retirement age of baby boomers finally here, a new era of estate planning is upon us. This era provides opportunities to create sound estate plans, promote and sell life insurance and long term care insurance, and reduce clients' taxes: a solution where everyone wins.

The death of the defined benefit pension has left the Boomers with large 401(k)'s, 403(b)'s and IRA's. This form of retirement has benefits, the ability to pass it on to generations; and detractions, the limited ability to maneuver it safely and easily during lifetime.

The average baby boomer now retires with assets in excess of $1 million. This, of course, can cause an Estate tax problem in New York. Also at risk, however, is the income tax associated with the IRA.

Because the assets are comprised partially or substantially of the IRA, the ability to protect the assets for taxes is difficult. It also provides complicated issues when dealing with nursing home protection. We are developing new solutions for the unique issues raised by the Boomers.

One of the solutions is to create an ILIT (Irrevocable Life Insurance Trust) for those people facing tax and asset protection issues. We may also create a Medicaid Trust in addition to or in lieu of, the ILIT. We fund the ILIT with reasonable permanent life policies ($150-500k), which will more than cure the estate taxes, but in some instances, also the income taxes.

What most clients don't realize is that they will be taxed on 100% of their IRAs for estate tax purpose. Yet, they only actually own 70 to 80% of those because the income taxes have not yet been paid. Clients generally find that being taxed on the government's money is more painful that paying taxes on their own. An ILIT is a simple and reasonable way to fix that dilemma.

The technique uses RMD's (or other draw-downs) to pay the annual premium. The tax is paid on the draw-down, thus reducing both the taxable estate and the income tax liability. This, in turn, enhances the funds "outside the estate." These transfers are further leverage by using life insurance to increase the value of the ILIT.

If a person is not insurable, this technique can be used to directly fund assets to the trust using the annual exclusion amount with withdrawal ("Crummey") powers. This is not enhanced by leveraged life insurance, but does have a positive effect on the estate.

The fear of long term care insurance costs has caused insurance companies to find new ways to provide palatable long term care coverage. The new "hybrid" policies that incorporate LTC benefits within life policies, hold great potential to both clients and those who sell the policies. Selling a policy that will pay a benefit no matter what happens to the covered person (death or chronic care) means that it can be sold as a "use it or use it" policy as opposed to the LTC "use it or lose it" dilemma. More people might be willing to pay the premium if they know they are covered for long term care and death, regardless of which happens.

The boomers are providing us with new opportunities to plan for them. The issues are challenging, but if properly promoted, the client, the attorney and the advisor all receive positive results.

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FAILING TO INCLUDE SUPPLEMENTAL NEEDS TRUSTS: A DISASTER IN THE MAKING

In recent months I have been faced with cases where proper planning could have saved families thousands of dollars. The federal government, as well as New York State, have created statutes that protect disabled persons. These statutes are intended to enhance the life of those disabled. The result of these statutes is the ability of families to protect assets and provide positively for those relatives.

If you have a client with a disabled child, and that child receives a direct inheritance, that inheritance will be required to be spent down to the allowable limit for their benefits (usually between $2,000 and $13,800). Until it is spent in this hasty fashion, the disabled person's benefits will be cut in whole or in part. It also means that the inheritance will be no longer there for their benefit. While it is true that in some instances a First Party Supplemental Needs Trust can be created, that type of trust does not have the same benefits as one created by a parent in their will or trust.

A testamentary standby supplemental needs trust should be included in all sound estate plans. This will cover the possibility that someone might become disabled in the future.

However, if there is a current disability, an SNT must be included in the estate plan to protect that person. It is not sufficient to create a discretionary trust, it must be a supplemental needs trust as defined in the federal and state statutes to proved the protection that is required.

Once a trust has been created and it is properly funded, the assets can be used for the benefit of the disabled beneficiary for anything except shelter (housing costs, including utilities) or food. Those costs are to be covered by the various benefits the disabled beneficiary is receiving from the state. Therefore, travel, entertainment and other expenses can be funded by the trust. Upon the death of the disabled beneficiary, the assets may pass to other family members.

During the lifetime of a disabled person, a first-party supplemental needs trust should be considered to receive any excess income or any payments, settlements or other inheritances the disabled person might receive.

No matter what the circumstances, planning for disabled or potentially disabled beneficiaries is critical to protecting family wealth.

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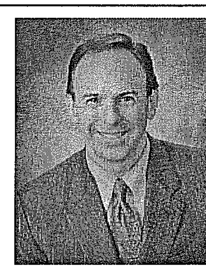
Tax Code changes will be addressed in a special edition.



UPCOMING TOPICS:

- Life Insurance and Medicaid Planning.
- The 2011 Tax Changes – where we go from there.