

THE WALSHLAW REPORT

Advisors in Estate Planning, Elder Law, Taxation, Business Law

Fall/Winter 2010

A REAL MESS – AND A WINDOW OF OPPORTUNITY

In the early days of the Bush (#43) Administration, Congress enacted the Tax Relief Reconciliation Act of 2001 (“the 2001 Act”), which gradually increased the federal estate tax exemption, and temporarily repealed the federal estate tax altogether. The 2001 Act, however, also included a sunset provision to the effect that all of its terms (including income, estate, and gift tax provisions) would automatically expire at the end of 2010.

Combined with prior legislation the 2001 Act recently produced the following estate tax exemptions and rates:

<u>Year</u>	<u>Exemption</u>	<u>Max. Rate</u>
2009	\$ 3,500,000	45%
2010 (repeal of estate tax)	\$ ∞	0%
2011 (and beyond) (sunset of 2001 Act)	\$ 1,000,000	55%

The 2001 Act was structured in such an arcane way because of Congressional rules that any revenue changes are evaluated over a ten-year time frame. By back-loading the more significant exemption increases and eliminating the estate tax entirely in the final year of the Act, the revenue projection numbers worked, and the Bush Administration could claim that it had achieved one of its high priority agenda items, the repeal (albeit temporary) of the death tax.

Throughout the first decade of the 21st century, the pundits and commentators were unanimous in their belief that the effects of the 2001 Act in 2009 through 2011 produced such drastically different results that “certainly” Congress

would fix this mess in one manner or another before 2010.

Several times in mid-decade, Congress almost came up with a plan to “fix” the estate tax, but failed to achieve consensus over (1) whether to set the exemption at \$3,500,000 or \$5,000,000, and (2) whether the top rate should be 45% (as favored by Democrats) or 15% (as favored by Republicans).

Despite the dim prospects for consensus while Congress was pre-occupied with health care reform, even in 2009 most commentators still believed that at the very least Congress would enact a “patch” to extend the 2009 estate tax rules to 2010 until they could come up with a permanent solution. After all, they couldn’t really actually let the estate tax expire, could they? Especially when it would be followed by a substantial decrease in the exemption and hike in rates in 2011.

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Well, they could and they did, and here we are trying to sort through this mess. We have always tried to write our documents to follow a formula that is designed to be as self-correcting as possible, so most of our clients’ documents don’t necessarily need to be revised. One exception may be those married couples who still have not revised their documents to reflect the “de-

coupling” of the Maryland and federal estate tax systems that occurred in 2004.¹

Even though one’s documents don’t necessarily *need* revision, that doesn’t mean that one *shouldn’t* take some steps before the end of 2010 to take advantage of unique opportunities that this gap in the estate and generation-skipping transfer (“GST”) tax laws affords.

To take full advantage of the estate tax opportunities available in 2010 requires one to die this year. We have not met any clients who are willing to take such a drastic step to save federal estate taxes for their family. But 2010 does present some long-range opportunities to avoid GST tax.

In an earlier newsletter, we discussed the advisability of creating a “dynasty trust”, i.e., a trust that won’t necessarily be distributed outright completely to children or even grandchildren, but which will be controlled by them with the assets to be used as needed.² In brief, instead of a traditional estate plan that would subject a family’s wealth to estate taxation at every generation level, the dynasty trust exposes the family’s wealth to tax only once, then removes that wealth permanently from the estate tax system.

One of the contributing factors to the advisability of the dynasty trust was the increase of the GST tax exemption from \$1 million in 2003 to \$3.5 million in 2009. The GST tax is a separate and additional estate tax that applies when a lot of property goes down two or more generation levels below the transferor. But, the GST tax exemption is measured by the value of what initially went in to the trust, not by what eventually is distributed out of it. So if \$3.5 million is

placed in such a trust today, and \$70 million is distributed from the trust to great-grandchildren 60 years from now, the whole amount still escapes any additional estate tax or GST tax.

This analysis is even more compelling during a window of time (2010) in which there is no GST tax at all. For a married couple with a large estate, one spouse can create a lifetime “marital trust” for the benefit of the other spouse. Properly structured to take advantage of the exemption of transfers between spouses from the gift tax, the creation of this trust would not trigger any gift tax. The property in the marital would, however, be included in the gross estate of the donee spouse upon his or her subsequent death. However, we could elect to treat the marital trust differently for gift and GST tax purposes. That is, we would essentially elect to ignore the gift for gift tax purposes, but elect NOT to ignore the gift for GST tax purposes, so that the donor spouse would be treated as having made the transfer to the trust for GST tax purposes - in the one year in which there is no GST tax.

Some commentators have suggested that the result is so dramatically favorable for taxpayers that Congress will be tempted to make retroactive changes to the GST tax law to eliminate this device. First, Congress has almost never made estate tax law changes that had retroactive effect, and we believe that they would be unlikely to do so in this area. Second, even if the law was changed retroactively, the type of trust that we envision would have sufficient flexibility built in so that at worst taxpayers would be no worse off than if they had done nothing.

We approach a mid-term election this fall, of course, and we know well that elections have consequences. Nonetheless, we think that the best-case scenario is the federal estate and GST taxes will be reinstated in 2011 with an exemption in the \$3,500,000 - \$5,000,000 range. Our worst case scenario, however, is that those taxes

¹ See “Maryland Estate Tax Changes”, *THE WALSHLAW REPORT*, Fall 2004.

² See “Creating Your Own Dynasty”, *THE WALSHLAW REPORT*, Winter 2009.

will come back with an estate tax exemption of only \$1,000,000, snaring significant taxes from the estates of thrifty individuals who led a middle-class lifestyle. We saw a recent unscientific poll of estate planners on the subject; 68% of those estate planners now believe that this worst-case scenario will be realized in 2011. After all, all that has to happen to get the worst-case scenario is for Congress to do nothing to fix the problem.

Even if the best-case scenario is realized in 2011 and your estate ends up escaping partial confiscation through taxation, setting up certain trusts now can lock in exemptions that we know are currently available. Not taking advantage of current opportunities can leave those assets at risk.

Our advocacy of the dynasty trust is based upon our belief that given current demographic and government spending and revenue patterns, taxes of almost every nature will almost certainly increase, both as to rates and to the scope of those taxes. Most of our clients worked very hard their entire lifetimes to accumulate their wealth, and paid taxes on their earnings throughout their lives. Some politicians, however, view the estate tax as a tax on dead rich people, from whom they feel they can raise revenue with little political repercussion. The dynasty trust allows one to remove significant wealth permanently from the estate tax system. Wherever feasible, we believe that permanently removing property or income from our clients' tax bases is a good thing.³

Albert Einstein once remarked that the most amazing force in the universe is the power of compound interest. Based upon some reasonable growth and tax assumptions, we recently

projected for one client that, even if estate taxes have to be paid upon his death, sheltering those assets from estate taxes in his children's and grandchildren's estates will leave his family with almost six times as much wealth than if that property had been subject to estate tax in the children's and grandchildren's estates.

This is a very generalized discussion of one possible estate planning device. If you are interested in learning whether this device (or something else) is advisable in your particular situation, please contact our office.

- James D. Walsh, Esq.

**Walsh & Company, P.A.
Suiing Your Needs In The
Following Areas:**

Estate Planning: Wills & Trusts
Probate & Trust Administration
Executor & Trustee Services
Senior Services & Elder Assistance
Medical Assistance Planning
Elder Law
IRS Tax Disputes
Tax Preparation
Business Planning & Organization
Real Estate
Contract Drafting & Disputes
Advocacy

³ For a similar analysis in the income tax area, see "Roth IRA Conversions - On Sale in 2010", *THE WALSHLAW REPORT*, Fall/Winter 2009.

Elder Law Corner

Untangling the Elderlaw Web

If you have ever spoken with an elder law attorney, a caregiver facing concerns about an elderly patient, or have had your own experience with loved ones in the twilight of life, you know about the tangled, complicated web of legal, medical, and emotional issues faced as we age. Health, wealth, personal values and family dynamics all mix together to present very unique circumstances for consideration.

The approach to understanding the complex situations and needs of an elder, and correctly advising and implementing a plan for that elder, requires the correct team of professionals. The elder law attorney needs as much information about the elder as possible. Although there are always gaps in information and uncertainties requiring some element of improvisation in every elder law case, the client and family are relying on the attorney to help them decide what to do when time is of the essence. As the attorneys, we rely on the elder, the elder's spouse, children, or close and trusted friends (all possible agents for the elder) both the initial interview, and in subsequent interviews, to gather necessary information and insight necessary for the most effective representation and advocacy on behalf of the elder.

The first question the attorney must ask is for what purpose the elder contacted a professional. It is important that the representation be carried out to address the elder's concerns, and not those of children, relatives, or friends.

At the first interview, the elder, or, their agent with the elder's permission, should do the following and bring the following items:

1. Give the attorney an adequate notion of the state of the elder's health. Has the elder had any health concerns such as heart problems, diabetes, stroke, surgery, etc.? Is the elder competent? Can they execute documents? If not, is there a guardian? Does the elder require assistance with daily tasks?

2. Compile and deliver complete personal and financial information about the elder, including sources and amounts of income, real estate and how it is titled, deeds, bank accounts and how they are titled, retirement accounts and beneficiaries, brokerage accounts and beneficiaries, insurance policies (life, health, disability, long-term care) and beneficiaries where applicable, annuities and beneficiaries, bonds or other assets, tangible personal property such as automobiles or collectibles and their value, liabilities and debts, statements, any existing legal documents such as wills, powers of attorney, living wills, advance health care directives, or trusts, any prepaid burial plots or funeral expenses, the names of individuals the elder would like to handle his or her affairs, and anything else that may be relevant.

3. Be ready to present what amounts to a biography of the elder: how long the elder was married, when did their spouse die, were there prior marriages and how did they end, names of children (both living and deceased), and any ongoing concerns in the family such as substance abuse, criminal conduct, poor financial management, and so on.

Certainly this is probing for a substantial amount of information. Without the information readily at hand, however, the attorney or the elder is limited to a certain element of guesswork in deciding what the best course of action is.

If all the information listed in this article is brought to the attention of your elder law

attorney, much of the guess-work will be removed. Understand that attorneys are professionals and ask for information because we need it to do our jobs to help protect the elder and his or her estate.



FACING FACTS - Talk To Your Parents About Estate Planning

It is 10:30 P.M., do you know where your children are? Are they in bed, sleeping peacefully, while you worry about ongoing issues with caring for your aging parents? If this sounds familiar, you are a card-carrying member of the “Sandwich Generation.”

In caring for (or anticipating the need to care for) your parents, you have probably already thought, “What do I do to make sure my kids don’t have to do this with me?” You are worrying about whether your parents have enough saved to last the rest of their lives, whether they will need to sell the home, whether you can avoid placing them in a nursing home, and whether you can afford to help subsidize their needs while continuing to meet your own. And, just as you do with your parents, you worry about the same concerns in your own life.

There are many things that you can do with your attorney and other trusted advisors to help plan for and insure against these concerns. With a properly drafted “testamentary special needs trust” (a trust that is formed after one spouse’s death for the benefit of the surviving, disabled

spouse), assets can be preserved to supplement public benefits available to the elderly, maximizing the dollars available for the surviving spouse’s long-term care. Wealthier families can give funds away during healthier years, rendering funds unexposed to medical assistance liens from the State while retaining enough money to take advantage of the trust options that are available.

You can talk to your parents about this, too. The important thing to remember, and to demonstrate to them, is that estate planning is about them more than it is about you. One principal goal in “elder law”, the growing field that focuses on legal issues affecting the elderly, is to make sure that the clients do not outlive their money.

Often, estate planning is seen only as a way to minimize taxes owed at death and to maximize inheritance for the next generation. That is very nice to be able to do, but growing costs of health care and longer life spans are making it just as possible that our bodies will outlast our dollars saved. With some advance planning, we can be proactive, not reactive, and ease the concerns and burdens placed on ourselves and our loved ones.

So, for those of you in the ‘sandwich generation’, it makes sense to think with your parents about estate planning and elder law issues. Time may be on your side and you can take longer strides in helping prevent your children from facing the same concerns that you face with yourself or with your parents. It may be easier for your parents to face events that are more imminent in their lives if their closest loved ones face the issues with them.

At Walsh & Company, P.A., our attorneys stand ready to consult with you, your parents and, if appropriate, your grown children, to help you navigate the maze of issues that face all of us as we age. – ***Barrett R. King, Esq.***

BLOGGING! ***Firm's Newsletter Finds Its Way Online***

Here at Walsh & Company, P.A., we pride ourselves on helping our clients remain up-to-date on what is happening in the legal world around them. So much information flows through us on a daily basis, it is impossible to process it all. In years past, we have provided a newsletter, *THE WALSHLAW REPORT*, to our clients by mail and during visits to our office in Columbia, Maryland. Today, Walsh & Company takes a step in the direction of allowing our clients more frequent access to updates in the estates and trusts arena by creating the online edition of *THE WALSHLAW REPORT*.

While the paper version of the *REPORT* is written on a roughly semi-annual basis, the online edition will be more frequent and, consequently, posts will cover one topic at a time. It is our hope that you will take advantage of this resource whether you are an existing client or not! Please subscribe to our feed or via email using the sidebar to keep abreast of updates to our blog.

To find: **BLOG** is located on our website. Go to home page, yellow menu bar, click far right item.

To receive the paper version of *THE WALSHLAW REPORT* via email, please send your email address to info@walshlaw.com

9841 Broken Land Parkway
Suite 206
Columbia, Maryland 21046
410-312-5690 • 800-480-6365
www.walshlaw.com

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