Legal Matters®

Estate Planning
winter 2015

How to help your trustee make good decisions for your family

As Yogi Berra supposedly said, "It's hard to make predictions, especially about the future." Yet when you create a trust for your heirs, you have little choice but to make predictions about what their needs will be many years down the road.

Because circumstances change, it's a good idea to make your trust flexible enough to accommodate the unexpected. If you tell your trustee what to do in too much detail, the trust might end up being useless or counter-productive if something unforeseen happens.

That's why most trusts give trustees quite a lot of discretion. For instance, a trust might say that a trustee can make distributions to a spouse to help maintain his or her lifestyle, or to children for their health, education and support. But it's up to the trustee to decide when and in what amounts these distributions should be made.

On the other hand, vague terms like these can sometimes be a problem. For instance, if you're a trustee, how would you handle these dilemmas?

- A surviving spouse wants more funds from the trust to help maintain her lifestyle, but this would deplete the trust assets, and when she dies, there will be very little left for the remainder beneficiary (a child of a previous marriage).
- A college student wants you to pay his tuition bills, since they're for "education." But he also wants you to pay for an "enriching" trip to Europe to travel, take classes, and gain experiences related to his major.
- A child quits her job because she wants to switch careers. She wants you to send her $5,000 a month as "support" until she finds a job in her new field.
- Another child gets married to someone who develops cancer and requires expensive medical care. The child wants you to pay some of the spouse's medical bills. However, the spouse isn't one of the named beneficiaries of the trust.
- Yet another child claims that distributions for "health" should include not only medi-


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New danger when doing IRA rollovers

The new IRA problem has a simple solution – but you have to be very careful to handle it properly, or it could result in big tax penalties.

There's now a big danger if you're rolling money over from one IRA into another IRA, as a result of a decision from the U.S. Tax Court.

Under federal law, you can only do one IRA-to-IRA rollover per year. If you try to roll over more than one IRA in a 365-day period, it's considered a distribution, and you'll be subject to significant taxes and penalties.

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In the past, the IRS has told taxpayers that this means you can't roll over the *same* IRA within a year. So if you rolled your Fidelity IRA over to Schwab, and you later wanted to roll the same IRA over to Vanguard, you had to wait at least 365 days.

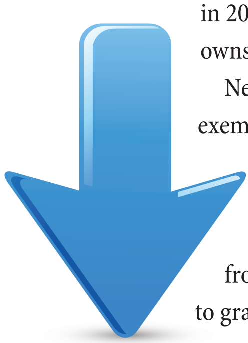
But the Tax Court says this is wrong, and in fact you can't roll over more than one IRA per year even if they're *different* IRAs.

So if you had two IRAs at Fidelity, and you wanted to roll them both over to Schwab, you'd have to roll one over, and then wait a whole year to roll over the second one.

There's an easy solution to this problem: Instead of rolling the funds over (having them made payable to you and then depositing them at the second institution), move them with a direct trustee-to-trustee transfer. As long as the funds move directly to the second institution, and you never touch them, it's not considered a rollover.

But you have to be very careful and make sure that the formalities are followed and the first institution doesn't actually send you any money. Otherwise, it could be a tax nightmare.

Eight states are easing their estate taxes in 2015



Eight states are reducing their estate tax burden in 2015, which is good news for anyone who lives or owns property in those states.

New York and Maryland are increasing their exemption amounts (the amount of assets an estate can have before any tax is due). For 2015, the New York limit goes from $1 million to just over $2 million, and the Maryland limit goes from $1 million to $1.5 million. Both states plan to gradually raise their limits to the amount of the federal limit by 2019. (The federal limit was $5.34 million in 2014 and will be $5.43 million in 2015.)

Tennessee's limit will be $5 million in 2015, and the tax will be repealed altogether in 2016.

Rhode Island's limit will go from about $1 million to $1.5 million next year, and Minnesota's will rise to $1.4 million, increasing gradually to $2 million in 2018.

Also, starting next year, the exemption amounts in Rhode Island, Washington, Hawaii and Delaware will be indexed each year for inflation.

Some gifts to charity should be made now, not in your will

In the past, many people's wills included a sizable donation to charity. Because the federal estate tax was so burdensome, including charitable bequests in a will was a good idea since it reduced the amount of tax the estate had to pay.

Now, however, the federal estate tax applies only to estates of well over $5 million. As a result, for a great many people, leaving money to charity in a will no longer provides any tax benefit.

On the other hand, the federal income and capital gains taxes have gone up, new surcharges have been added on investment income, and many states have raised their income and capital gains taxes as well. As a result, many people could reap significant tax savings if they made planned annual gifts to charity while they're alive, as opposed to making bequests in a will.

If you have an older will that includes a significant charitable bequest, this might be a good time to reconsider whether you could save taxes by writing the charity out of your will and instead making regular donations each year.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cal care, but also a gym membership, yoga classes, acupuncture, spa treatments, a hiking trip, and a three-day meditation retreat.

You can see the problem: The trustee has become a de facto parent, acting as arbiter of the beneficiaries' needs and lifestyle choices. And the trustee must somehow do this while being "fair" to everyone and not spending so much that the trust runs out of assets.

One way to help with this situation is to give the trustee a lot of discretion in the trust document, but then write a separate "letter of intent" spelling out your hopes, dreams, goals, rules and limits regarding your family. This letter may not be legally binding, but it can be very useful to a trustee in making decisions.

For instance: If the trust will benefit one generation and then another generation, roughly how much money should be left for the second generation? Should the needs of one generation take precedence over the other? Are there circumstances where you'd make an exception – say, if someone develops an expensive illness?

If the trust will benefit several children, is it important to you that all the children ultimately receive a similar amount of the assets? Or can the trustee provide more to a child who has a greater need? And can distributions to children take into account the needs of their own family members?

Do you want your children to have relative comfort in their youth, and to take advantage of the experiences that comfort can provide? Or is it important to you that they earn their own way? And if one child is highly responsible and another is a spendthrift, is it okay for the trustee to treat them differently?

A "letter of intent" doesn't have to be written in legalese, and you can revise it from time to time. Obviously, it can't cover all possible issues – but it can at least give a trustee some clues as to what to do when he or she is asked to fund a new car or a backpacking trip across Italy.

A 'letter of intent' can't tell a trustee what to do in every case, but it can provide important guidance to keep your family on the right track.

Saving taxes with WINGs, NINGs and DINGs

Some taxpayers with large state income tax bills have been trying to avoid them through the use of out-of-state trusts.

These trusts have been created in three states that have no or minimal state income tax – Wyoming, Nevada and Delaware. The idea is that people in high-tax states can set up trusts in these low-or-no-tax states to hold the investments that produce the income.

The trusts are called "incomplete non-grantor gift trusts." A Wyoming incomplete non-grantor gift trust is known by the acronym WING. In Nevada and Delaware, there are NINGs and DINGs.

In theory, you can put income-producing assets into a WING, NING or DING and be an income beneficiary. You'll pay no federal gift tax on the transfer to the trust, and no state income tax on the income you receive.

That's the theory. In practice, some high-tax states (such as New York) hate this arrangement because they're losing tax revenue. So they're changing their laws in an effort to tax WING, NING and DING income. (According to the New York tax authorities, some $1.5 billion in income a year is being generated by assets in these trusts – and that's just the assets owned by New York residents.)

The IRS is looking at these trusts, but it hasn't given a conclusive answer about the tax consequences.

Another problem is that, to avoid the tax, you can't have too much control over the trust. Generally, while you can be an income beneficiary, there must be other beneficiaries who also have a say on distributions, and there must be a trustee in the state where the trust is set up.

Out-of-state trusts have been particularly popular with people who are selling large appreciated assets, such as a family business. The idea is to transfer the asset to a trust prior to the sale.

However, because the law is unsettled, these trusts can be very risky. They're certainly not for everyone, and they require careful thought and planning.

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Inherited IRAs are not protected from creditors

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If you're planning to leave an IRA or other retirement account to your heirs, you might want to consider creating a trust to hold the account. That's the upshot of a recent ruling from the U.S. Supreme Court.

That's because IRAs that are inherited from anyone other than a spouse are no longer protected from creditors in a bankruptcy.

Heidi Heffron-Clark and her husband Brandon filed for bankruptcy after their pizza shop failed in 2009. They owed their landlord $74,000, but didn't have enough cash on hand to pay the debt.

Heidi did, however, have $293,000 in an IRA that she inherited from her mother.

In general, IRA funds are exempt from creditors in a bankruptcy. Congress created this rule in order to protect Americans' retirement savings and to prevent elderly people from not having enough to live on.

But the Supreme Court made an exception, and said this rule doesn't apply to *inherited* IRAs – at least if they were inherited from someone other than a spouse. Inherited IRAs are different, the court said, because the owner didn't actually contribute any funds to them, and simply received them as a kind of windfall.

Therefore, Heidi's IRA could be tapped to pay off the landlord.

As a result, if you're planning to leave an IRA to your children or other heirs, and you want to protect the funds in case your heirs rack up business or personal debts or get sued in a lawsuit, you might want to leave the IRA to a trust instead.

A trust might not be absolutely foolproof, but it provides much better protection than simply leaving an IRA to someone directly.

Although the Supreme Court case involved an IRA, the same principle might well apply to other sorts of retirement plans such as 401(k) and 403(b) plans.