



Laws and Life Keep Changing

Important changes in the law and other developments have significantly affected estate planning. Almost everyone who created an estate plan prior to these changes will find their plan needs to be reviewed and updated. Also, as time goes by, family situations change, so the estate plan may be out-of-date in terms of who gets your assets when you die, when and how they get the assets and who will be in charge of administering those decisions when you are gone. Following are five developments that necessitate revisions to existing estate plans:

Divorce and Creditor Protection

With the continuing proliferation of lawsuits, and the divorce rate at about 50 percent, parents and other donors are using trusts to pass assets to their children and other heirs, in order to protect the assets from such problems. These trusts can be either “inter vivos” trusts (i.e., created while the donor is still alive) or testamentary trusts (i.e., trusts created by

the will when the donor dies). However, some of the “do-it-yourself” trusts and “bargain-priced” trusts do not adequately provide these protections. Make sure that your trust does. Make sure it has adequate “spendthrift” and “trustee holdback powers” so that the following trust benefits will be preserved for your beneficiaries:

>> Lawsuit protection, if the trust is

properly structured.

>> Protection from a divorcing spouse of a child or grandchild beneficiary.

>> A reduction (or elimination of) estate and generation-skipping transfer taxes.

>> In the case of a “spendthrift” beneficiary, or one who is prone to drug, alcohol, or gambling addictions, the ability to have a trustee manage the assets for the beneficiary.

>> In the case of a “special needs” beneficiary, the ability to maintain his or her eligibility for valuable government benefits (such as Medicaid or Social Security Disability) even though the trust provides funds for the beneficiary’s supplemental needs.

Having the assets held in a trust for a beneficiary does not mean that they are “locked up” and cannot be used to help the beneficiary. Rather, the trustee of the



Five Vital Signs for Healthy Wills and Trusts

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trust can use the assets to help with the child's or grandchild's education expenses, church missions, purchase of a home or anything else the parents or other donors choose. At the same time, however, the assets are not available to the child's or grandchild's creditors, legal problems, divorcing spouse — or his or her own poor judgment and spending decisions.

Also, be aware that if you have a will — including a will with testamentary trust provisions — instead of an inter vivos trust, wills have to go through probate court when you die and, generally, inter vivos trusts do not.

Asset Protection Through Life Insurance

Utah recently enacted a law enabling Utahns to protect life insurance cash value and death benefits from creditors. The

new law can be an asset-protection tool that can bring financial security to those who utilize it. To illustrate the usefulness of this tool, assume you have been saving money for many years in checking, savings and stock brokerage accounts, and stocks, bonds, real estate, or any other number of investments. If you are sued (as a result of a traffic accident, professional liability, etc.), and the creditor proves you are liable to him, he will have a court judgment against you. If the judgment amount exceeds your applicable liability insurance coverage, the creditor will try to satisfy the remainder of his court judgment from your personal assets.

Prior to 2005, there were not very many assets you could protect against creditors with court judgments. For example, if your home was worth \$250,000, a creditor could force its sale, take the sale

proceeds and leave you with \$20,000. Under this new insurance-policy law, you have the opportunity to accumulate an unlimited amount of cash in your life insurance policy(ies) and keep it exempt from future creditors.

Be aware, however, this new law is not merely a new life-insurance product for sale. It is a law that needs to be explained by your asset-protection attorney before the strategy is implemented. For example, if you were to start putting money into a life insurance policy knowing that a specific creditor may be pursuing you, that could undermine the exemption and expose the money to the creditor's grasp.

Medicaid Planning

Nursing home and other long-term care costs can be financially catastrophic to people's savings and financial security.

Medicare or other health insurance policies do not cover such costs. The average cost for such care is in excess of \$50,000 annually. In just five years the bill could exceed \$250,000. These bills are generally paid for in one of three ways: 1) long-term care insurance; 2) directly from your income and assets; or 3) Medicaid and other public assistance programs.

If you need long-term care that is not covered by long-term care insurance, you will have to spend all of your assets and savings (except for about \$2,000 and a few other minor exceptions) before Medicaid will assist you. This could be tragic because you have worked hard all your life to save and have financial security for yourself and your family, and that security can completely vanish as your assets are consumed for your long-term care.

A properly designed trust and power of attorney should contain special provisions to allow the trustee of your trust (and your power of attorney agent) to engage in certain planning strategies to allow you to qualify for Medicaid and other assistance programs without depleting all of your assets. These provisions are sometimes referred to as “Medicaid Triggers” and include the ability to transfer ownership of assets from your trust and estate to your loved ones (or into “safe” entities for your loved ones). Without those Medicaid Triggers, trusts generally prohibit trustees from making those types of transfers. Medicaid Triggers enable the trustee to transfer assets to your spouse, convert assets to Medicaid-exempt property or purchase certain kinds of special annuities that keep the door open for Medicaid eligibility. If your trust is designed properly and you become incapacitated, a great portion of your assets can be protected against the Medicaid “spend-down.”

These Medicaid Triggers do not guarantee that you will qualify for Medicaid. Consultation with a qualified attorney is critical to make sure your family has the right strategy and correct legal documents to achieve Medicaid eligibility.

Distribution Rules for IRAs and Other Retirement Plans

New rules for distributions from IRAs, 401(k)s, 403(b)s and other “qualified” retirement plans make it easier for savers to take advantage of the “stretch IRA” concept. Under the new rules, your beneficiary can enjoy a deferred payout of the retirement plan funds over his or her life expectancy. That enables the beneficiary to further defer the income taxes that have already been deferred as you have been contributing to the plan or account.

The new rules now permit a trust to be the beneficiary of a retirement plan without losing these most important income-deferral opportunities — but only if the trust is a “qualified” trust. This means that the trust must comply with specific federal laws and regulations. If the trust is qualified, the trust beneficiaries are entitled to stretch withdrawals from the IRAs, 401(k)s, 403(b)s and other qualified plans nearly the same as if the trust was not the beneficiary.

If a non-qualified trust is the beneficiary of such retirement plans, that triggers payment of income taxes after your death — taxes that could have been deferred if the trust was qualified. Some people may think it’s easier to just name non-trust beneficiaries as beneficiaries of retirement plans and accounts rather than worry about whether their trust is “qualified” or not. That’s true. It is easier, but not necessarily better. Without the trust you lose the opportunity to have your trust protect your retirement assets (as described in the Divorce and Creditor Protection paragraph on page 72).

Tax Relief Act of 2001

In June of 2001, President Bush signed the Tax Relief Act of 2001. Among other things, the Act dramatically changed the federal estate tax. One of the primary changes is the increase in the amount you are permitted to pass to your heirs at your death without paying any estate tax. Some affects of this Act are:

>> Estate planning documents must conform to changes in the estate tax exclusion, gift-tax exclusion and

generation-skipping transfer-tax exclusion.

>> Documents must anticipate the proposed elimination of the “step-up” in basis for capital gains assets.

Another important provision of the Act is its “sunset” provision. Although the new law was very tax-friendly to Americans, it will all be automatically repealed in 2011 (and the old unfriendly estate tax law will return) unless Congress votes to make the 2001 changes permanent. Given federal budget deficits and political pressures, that vote currently appears unlikely. Therefore, estate tax planning has to be done with one eye on pre-2001 and the other eye on 2011. Utahns are well-advised to stay in touch with their attorney who specializes in these tax matters.

Take Action

These important changes can have a profound impact upon you and your loved ones. Reviewing your estate plan (wills, trusts, power of attorney, etc.) every two years or so always makes sense, but when there have been changes as dramatic as those we’ve seen in the past four years, it becomes even more critical to make sure your plan has kept pace with these important changes. If your plan hasn’t been reviewed in the past two years, by an attorney who specializes in these matters, it is time to do something about it — for your peace of mind, and for the protection of your family and others.■

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