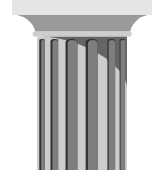


THE YEAR IN REVIEW

1996



The Newsletter of the Law Office of Christine J. Sylvester

December 1996

Preview Issue

To: Clients
From: Christine Sylvester

Welcome to a new tradition!! As those of you who receive this newsletter already know, this year brings to close a full term of operation as an estate planning and asset protection law office in the Charlotte area. This is my firm's first annual newsletter updating your knowledge on various legal issues and notifying you of upcoming services. For your information, I am now a member of the National Academy of Elder Law Attorneys (NAELA) and the Elder Law Section of the North Carolina Bar Association. NAELA's mission is to enable elder law attorneys to identify and meet client needs through the exchange of ideas and information on substantive elder law issues and the management of successful elder law practices. NAELA promotes improvement in substantive law, legal education, and ethical guidelines in serving older persons and serves as a key public policy advocate on behalf of older persons. In light of the recent activity in Congress, NAELA enables its member attorneys to provide up to date information and guidance on all issue related to our services. The North Carolina Bar Association granted section status to the Elder Law Committee in September 1996. For two years I served as a member of the Elder Law Committee, and was delighted to see our committee accepted as a section by the bar. The scope of this section addresses many areas of law such as insurance, housing counseling, income, estate and gift tax advice with a focus on North Carolina. I hope you enjoy the newsletter and, of course, should you have any questions, then please call Mandy, my assistant, for a consultation. I would like to take this opportunity to thank you for being part of my practice. I value each and every one of you as my client.

Recent Activity

Medicaid Eligibility for Nursing Care: In August of this year, Congress and President Clinton put in place a criminal penalty for certain transfers of property for purposes of qualifying for Medicaid. Under the old law, there was no criminal penalty for gifts given three years or more before a person applied for Medicaid. Now, the so-called look-back period has been extended from three years to five. And under the new rule, it will be a crime to make any transfer "with the intent to dispose of those assets to qualify for Medicaid benefits." The penalty: Up to one year in jail and a \$10,000 fine.

Irrevocable Insurance Trust One estate planning technique is the creation of an irrevocable life insurance trust, the Trustee of which purchases life insurance for payment of estate taxes. The Trustor contributes money into the trust and then the Trustee pays the premiums for the life insurance. At the time the Trustor contributes money to the insurance trust, a "Crummey" (taken from the name of a case) notice is given to a beneficiary of the trust which advises them that they have a present right to withdraw their share of the contribution (which they usually never do). This preserves the annual \$10,000 gift exclusion. In many cases, the Trustees have the beneficiaries waive their "Crummey" notices so notices did not have to be mailed every year. In a recent technical advice memorandum, TAM 9532001, the IRS stated that a

waiver by the beneficiary of their "Crummey" notice prevents the beneficiary from having an immediate withdrawal right and therefore no annual gift tax exclusion is available. Thus, Trustees should not have beneficiaries sign waivers.

A North Carolina Act to Describe Circumstances Under Which a Property Power Attorney-In-Fact May Make Gifts: This Act authorizes attorneys-in-fact to make gifts of an individual's assets to charities, to individuals other than the attorney-in-fact and to the named attorney-in-fact. Gifts to charities and to other individuals must be made "in accordance with the principal's personal history of making or joining in the making of lifetime gifts." Gifts to the attorney-in-fact must be expressly authorized in the document.

An Act to Exempt IRA's, Individual Retirement Annuities, and Simplified Employee Pension/Individual Retirement Accounts From the Claims of Creditors: This Act protects the above-stated accounts from the claims of creditors. This adds to the list of assets protected under North Carolina law for those asset protection conscious clients.

Increase in the Class A Inheritance Tax Credit. The Class A inheritance tax credit has been increased from \$26,150 to \$33,150. As a result of these changes, the "exemption equivalent" amount of property which can pass to a single Class A beneficiary free of North Carolina inheritance tax has been increased from \$500,000 to 600,000.

Recognition of QTIP Treatment for Property Passing to a Surviving Spouse. North Carolina now allows a marital exemption for North Carolina gift and inheritance tax purposes for a qualified terminable interest property ("QTIP") passing to a donee-spouse or to surviving spouse. As is true with the federal tax system, the QTIP property will be subject to North Carolina inheritance tax upon the death of the surviving spouse.

The Power of Charitable Gifting - A Truly "Painless Gift"

In the world of estate planning, can there be such a thing as a truly "painless gift?" Through the use of a Charitable Remainder Trust (CRT) and an Irrevocable Life Insurance Trust (ILIT), it is possible to execute a "WIN-WIN-WIN" estate planning transaction - the truly painless gift.

A CRT is an irrevocable trust established for some stated charitable purpose. The CRT is established under a trust agreement which sets forth the purpose of the trust and how the trust is to be administered. If the trust meets certain requirements under IRC 664, the trust will be exempt from income tax. Under the terms of the CRT agreement, the Trustor agrees to transfer property to the trust. The Trustee of the CRT in turn promises to make a stream of payments back

to the Trustor (Retained Interest). These payments can be made for the life (or lives) of one or more individuals and the payments are stated as a fixed sum or a fixed percentage. During the term of the CRT, the Trustee simply makes payments to the Trustor. Upon termination of the CRT, the remaining trust estate is generally distributed to the charity(ies) named in the CRT agreement (Remainder Interest). If the CRT meet the requirement of the IRC, a number of benefits can be achieved by transferring property to the CRT.

Immediate Income Tax Deduction - The Trustor receives an immediate income tax deduction equal to the Remainder Interest. The value of the Remainder Interest is determined actuarially using the Applicable Federal Rate (AFR). The deduction is subject to certain annual Adjusted Gross Income limitations, and can be carried forward for five (5) years.

Estate Tax Savings - The property transferred to the CRT will be excluded from the Trustor's estate for estate tax purposes. By using the increase in cash flow from the CRT to fund an ILIT, the net benefits received by the Trustor's heirs is increased.

Increase Cash Flow - The Trustor can transfer low-yield property to the CRT. The Trustee can then sell all or part of the property and use the proceeds to pay the Trustor a higher rate of return than he or she was receiving from the original property transferred into the CRT. This may enable a Trustor to convert an otherwise nonproductive asset into a valuable source of supplemental income.

Capital Gains Tax Savings - The Trustor can transfer property with large built-in capital gain into the CRT. No capital gains tax is paid by the Trustor upon the transfer. Because the CRT is tax exempt, the Trustee can sell the property without having to pay capital gains tax.

Benefit to Charity - Upon termination of the CRT, the Charity(ies) named in the CRT will receive a substantial benefit.

How Can Insurance Play A Role in the CRT Transaction?

The ILIT or "Wealth Replacement Trust" is the key component of the "WIN-WIN-WIN" estate planning transaction. It is the tool that makes the charitable giving transaction truly painless.

In brief, an ILIT is established for a purpose of owning life insurance (although the trust can also own other types of assets). Typically, each year, the Trustor of the ILIT makes cash gifts to the trust using his or her annual exclusions of \$10,000 per trust beneficiary. The Trustee of the ILIT uses the cash to purchase the policy and to pay the premiums. At the Trustor's death, benefits are not included in the Trustor's estate for estate tax purposes, and are received by the beneficiaries income tax-free.

As noted above, the Trustor of the CRT can increase his or her cash flow by transferring low-yield property or substantially appreciated property to the CRT. By using the increase in cash flow to fund premiums on the policy owned by the ILIT, the value of the assets transferred to the CRT will be replaced at the Trustor's death and the Trustor's heirs will receive the value estate tax free.

**The Trustor, the Heirs and the Charity(ies)
ALL WIN!!!**

I know many of you have read, heard or seen information regarding charitable gifting and the numerous tax, emotional, societal and family benefits associated with that level of planning. We are presently planning an informational seminar as an informal introduction to how such planning may personally benefit your estate planning and lifetime objectives. These informal sessions will be held in small groups and we are presently planning one small session in December and one in January. Please feel free to call if you would like to make reservations.

Estate Checklist - All clients reading this newsletter should answer yes to the following questions.

1. I have discussed with my spouse and family my overall estate planning objectives and where the original documents are located.
2. I understand the trust process and decisions I will have to make following the death of my spouse.
3. I and my family know immediately where to go for the following advise:
 - a. Legal
 - b. Banking
 - c. Accounting and taxes
 - d. Life insurance
 - e. Business interests
 - f. Real Estate investments
 - g. Stocks, bonds & other financial instruments.
4. I have reviewed with my spouse the steps to be taken upon death.
5. I have discussed with my spouse all of my pension, profit-sharing, retirement, key employee life insurance, and similar benefits.
6. I know where all important legal documents (military discharge papers, wedding and birth certificates, life insurance policies, financial records, etc.) are kept.
7. My spouse and I have fully discussed the use of trusts in our estate planning.
8. My spouse and I have discussed how to dispose of my/our business interests if one of us dies.
9. I have completely funded my/our revocable living trust.
10. I have reviewed our present financial standing and know to take additional action to protect our estate should it grow beyond \$600,000 per individual (1.2 million for a married couple).

HAVE A HAPPY HOLIDAY SEASON!!!

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This Newsletter is meant to advise you of recent changes in the federal tax and North Carolina law which may affect your estate planning and/or corporate and/or other matters. If any of this information affects your situation, then please contact this office. Because of the number of exceptions, no work may have to be done, but it is the mission of this office to advise you of any changes.