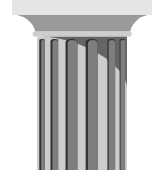


# THE YEAR IN REVIEW

## 1997



Lawrence & Sylvester, P.L.L.C. Annual Newsletter

April 1998

Second Issue

To: Clients  
From: Christine Sylvester

This is our annual newsletter updating you on our office activity as well as recent legal activity which may affect your estate planning. One exciting note within this office is the recent formation of the firm Lawrence & Sylvester, P.L.L.C. effective April 1st of this year. Scott E. Lawrence is a graduate of Wake Forest University School of Law (class of 1989), and has practiced in the Lake Norman area since 1992. His practice concentrates in the areas of corporate and business law, commercial real estate transfers and residential real estate transfers. Over the past year, Mr. Lawrence and I worked on quite a number of mutual cases. We found that our areas of concentration complemented one another very well. The firm will maintain two offices, one at Lake Norman at Exit 28 of I77, and a Charlotte office in the University area. In addition, starting May 15th, we will have a new south Charlotte office location across from Cotswold Mall at 135 S. Sharon Amity Road, #207. We are excited about this merger and together we will be able to provide a high level of service to our clients. In addition to estate planning, we are now able to provide quality representation in the areas of corporate and real estate law. This office is also pleased to announce the addition of a second attorney to our estate planning staff. Attorney K. Michele Woodside is a graduate of Campbell University School of Law (class of 1997) and served as the notes and comments Editor for the Campbell University Law Review as well as Business Editor for the Campbell Law Observer

In addition to the activity within our office, it appears that Congress had an exciting 1997. The scope of this newsletter will address the Taxpayer Relief Act of 1997 and its impact on the estate planning arena. 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 a part of our growing practice. I value each and every one of you as our clients.

### Taxpayer Relief Act of 1997

**Traditional IRAs:** The 1997 Tax Act increased the income you can earn without losing your IRA deduction. Your spouse may now make a fully deductible contribution to an IRA if he/she is not an active participant in your employer-sponsored retirement plan or has no other retirement plan of his/her own. The new break for spouses phases out for those with AGI between \$150,000 and \$160,000. Also, if you are working at age 70.5, you may postpone your IRA distribution until you retire. Finally, individuals may now withdraw money from their IRAs without penalty before the age of 59.5 if the funds are used to pay qualified higher education expenses or for the purchase of a first home.

**Roth IRAs:** Beginning in 1998, retirement savers have a new tax-favored alternative called the Roth IRA. This new IRA will not yield deductions when you put money in, but will result in a tax-free withdrawal so long as the funds have been invested for five years and the withdrawal occurs because you are over 59.5, disabled or a first time home buyer. Otherwise allowable contributions to Roth IRA's (up

to \$2,000 per individual per year) phase out for single taxpayers with AGI between \$95,000 and \$110,000 and for joint filers between \$150,000 and \$160,000 of AGI. Contributions are permitted even after you reach 70.5 as long as you or your spouse has earned income and there is no requirement that you withdraw once you reach age 70.5.

**Roth vs. Regular IRAs:** 1998 is the year to determine whether or not you wish to convert your traditional IRA into a Roth IRA. Rollovers from a traditional IRA to a Roth IRA are a taxable distribution. However, if converted in 1998, you may spread out that income tax bill equally over a four year period. Careful consideration should be given to the overall ramifications of such a conversion prior to acting. One important question to ask is how many years of tax-deferred earnings will it take to earn back the tax paid as a result of the conversion?

**Living Trusts and IRAs:** Many of you have a significant amount of your estate value within your IRA. From an estate planning perspective, it was always important to structure the beneficiary designations such that the ultimate amount of estate tax protection would be available. A previous concern in naming a living trust as the beneficiary was that the IRS did not view a living trust as a "person" therefore, upon death, if the proceeds of an IRA were made payable to a living trust, a lump sum income tax was required to be paid, losing future income tax-deferral. Under the new regulations, if certain requirements are met, when a living trust is named as beneficiary of an IRA, the beneficiaries of the living trust may be considered the designated beneficiaries to determine the payout of the IRA using the life expectancy of the beneficiaries named under the living trust. As such, no longer will a lump sum payment of income tax be automatically required when a living trust receives monies as the named beneficiary of an IRA. This opens up a whole new area of planning. We are now able to use the IRA if needed to fund the B trust (exemption equivalent trust) or control the payout to beneficiaries by naming the living trust as the beneficiary of the IRA and we do not lose the income tax advantages previously available only to individuals.

**Federal Estate and Gift Taxes:** More of your assets can be passed on or gifted to family members or anyone else free of federal estate or gift taxes. The amount exempted from federal estate or gift tax (which used to be referred to as the unified credit) in 1997 was \$600,000. Under the 1997 Tax Act the unified credit is now referred to as the "exemption equivalent" and will rise over a period of time as illustrated below:

<u>Year of Death</u>	<u>Exemption Equivalent</u>
1998	\$625,000
1999	\$650,000

2000	\$675,000
2001	\$675,000
2002	\$700,000
2003	\$700,000
2004	\$850,000
2005	\$950,000
2006	\$1,000,000

**ATTENTION: If you are a married client of this office in which A/B trusts were created within your living trust prior to 1998 and your total estate does not exceed 1.2 million, you need to contact this office so we may review your tax plan in light of this new exemption equivalent!!**

**Qualified Family Owned Business:** If more than 50% of a person's estate consists of qualified family owned business interests his or her executor can elect to exclude an additional \$675,000 of the estate from taxation. With the exemption equivalent at \$625,000 for 1998, an estate that qualifies for the additional business exemption may protect up to 1.3 million from taxation. For married couples, this means a protection of 2.6 million. With the maximum protection leveled at 1.3 million per individual, as the exemption equivalent rises, this business benefit will reduce. By the year 2006, the exemption equivalent will be at 1 million (see chart above), therefore the business exemption will only amount to \$300,000.

For all clients that own family businesses or farms, one item that you need to be extremely careful with in this area of estate planning is insurance. As noted above, to qualify for the family business exemption, more than 50% of your estate value must be in that business or farm. If you own insurance and you are making premium payments on that insurance, then the death benefit of that policy will be included in your estate value and could jeopardize your qualification for this business exemption. For example, lets assume that you own your home (\$200,000), investments (\$100,000) and stock in your family business (\$350,000). Your total estate value would be \$650,000 and 50% or more of that value is in the family business (\$350,000 of \$650,000 = 54%). Let's now assume that we also find an insurance policy that you own on your life which pays out to your children upon death \$350,000. If we now add in the insurance to your estate value, you have an estate worth \$1,000,000. \$350,000 of \$1,000,000 = 35%, therefore, by adding in the insurance, you do not qualify for the family business exclusion.

**CAREFULLY LOOK AT YOUR INSURANCE IF YOU WISH TO QUALIFY FOR THE FAMILY BUSINESS EXCLUSION.** If your present insurance, causes you to lose the business exclusion, you need to consider moving the insurance out of your estate by transferring ownership either to your children or preferably to an irrevocable trust. Please contact this office so we may discuss this further.

**Investors:** The top tax on long-term capital gain is reduced from 28% to 20% (to 10% for taxpayers in the 15% bracket). However, there are some tricky holding period rules to contend with in that you must hold the assets for eighteen months on the sale date to qualify, otherwise the old 28% rule applies. After the year 2000 the top tax rate for long term capital gains will be 18% (8% for taxpayers in the 15% bracket) if a five year holding period is met. The 18% rate (but not the 8% rate) will apply only if the holding period for the assets begins after the year 2000.

**Homesellers:** The major change affecting home ownership is the elimination of the old rules that had permitted taxpayers to roll over the gain realized on selling a home into a new or replacement home or

exclude up to \$125,000 of gain if over age 55. Instead, a single new exclusion is available without regard to your age. Under the new law, up to \$250,000 of home-sale profit is tax-free if the sale takes place after a person has owned the residence and used it as a principal residence for at least two of the five years prior to the sale. The exclusion is doubled to \$500,000 for married persons filing jointly. The new exclusion is allowable each time a taxpayer sells a principal residence, but generally not more often than once every two years.

**NOTE: When planning for the care of an ailing parent or other family member, some consideration should be given to these rules. It may be feasible that with modest additional home care, your parent may comfortably and safely reside in his/her home for the additional time period to qualify for, or increase, the home sale exclusion tax benefit. In addition, if you have an ailing spouse, consideration should be given to the selling of the home now to exclude \$500,000 of gain if needed. Upon death of the spouse, you will lose the \$500,000 benefit and only a \$250,000 exclusion will be available.**

---

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

1. My family understands the trust process and decisions they will have to make following my death.
2. I have discussed with my family all of my pension, profit-sharing, retirement, key employee life insurance, and similar benefits.
3. My family knows where all important legal documents (military discharge papers, wedding and birth certificates, life insurance policies, financial records, etc.) are kept.
4. My spouse and I have discussed how to dispose of my/our business interests if one of us dies.
5. I have completely funded my/our revocable living trust.
6. I have reviewed our present financial standing and know to take additional action to protect our estate should it grow beyond \$625,000 per individual (1.25 million for a married couple).

*Lawrence & Sylvester, P.L.L.C.*  
 2720 East WT Harris Blvd., Suite 100  
 Charlotte, North Carolina 28213  
 (704) 597-7337  
 (800) 914-9041  
 cjs@preservingyourwealth.com

*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.*