



KOSTNER, KOSLO & BROVOLD LLC
ATTORNEYS AT LAW

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ESTATE PLANNING

Arcadia, Wisconsin

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MEDICAL ASSISTANCE PLANNING

Many people consider protecting their assets from being used to pay for nursing home care to be a part of estate planning.

Medical Assistance is a government welfare program that helps pay for health care for people who cannot afford to pay for their health care. Medical Assistance (sometimes referred to as "Medicaid", "MA" or "Title 19") is different from Medicare.

Exempt Assets

A single person can own the following assets and may still be eligible for MA:

- A. Automobile up to \$4,500 value
B. Whole life insurance policy up to \$1,500 face value
C. Irrevocable burial trust up to \$3,000 value
D. Burial space (plot), head stone, casket, vault, crypt and other pre-paid funeral expenses
E. Personal property and furnishings of reasonable value
F. Liquid assets up to \$2,000 (e.g., bank account)
G. Home of no more than \$750,000 equity value (but only as long as applicant intends to return to it)

Married couples (one spouse in nursing home, one at home) can own the following assets and may still qualify for MA:

- A. Spouses can each own the exempt assets listed as A. through G. above, except that they may own only one (1) home but of unlimited equity value if home is occupied by spouse, minor child, or adult disabled child, and only one (1) automobile, but of unlimited value.
B. A spouse not in the nursing home can own the greater of \$50,000 or one-half of the couple's non-exempt ("countable") assets, up to a maximum of \$109,560.

Retirement assets in the name of the spouse living at home are considered exempt under the Wisconsin Supreme Court's decision in Keip v. State of Wisconsin in determining the nursing home spouse's eligibility for MA.

Special circumstances may apply if both spouses need MA to pay for nursing home care.

Divestment

The MA rules discourage people from giving away assets that they could use to pay for nursing home care. The rules discourage giving away or "divesting" assets by making a person who gives away assets that could have been used to pay for nursing home care ineligible for MA for a period of time.

currently \$6,216 per month in Wisconsin. This amount is adjusted at least annually.

When a person applies for MA, they must disclose any gifts or divestments they have made during the three (3) years before the application is filed. (This disclosure period will gradually increase to five (5) years by January 1, 2014.) Gifts made prior to January 1, 2009, are only subject to a 3-year disclosure period and will no longer affect someone's eligibility after January 1, 2012. Gifts made on or after January 1, 2009, though, will make the person and his or her spouse ineligible for MA to pay for nursing home care for up to five (5) years from the time of the gift. Because of this ineligibility rule, we recommend that a person not commit a divestment unless they have other assets available to pay for their nursing home care for up to five (5) years after the divestment.

Planning Options

In spite of the changes to the MA rules in recent years, there are still some planning options available:

- Purchase the exempt assets listed above.
- Sell a remainder interest in your home.
- Purchase a term life insurance policy without a cash value.
- Purchase long-term care insurance that qualifies under the Wisconsin Partnership Program.
- Purchase an annuity (a contract where a person pays an amount to an annuity company, which agrees to pay it back with interest over time). This planning technique can work better for married couples than for single individuals.

Additional Considerations

Other than the MA divestment rules, factors you should consider before you decide to transfer your assets include:

- After you give your property away, you no longer have the legal right to control it or sell it, or receive income from it.
- The person to whom you give your property likely will not have any legal obligation to provide financial assistance to you.
- The MA program could be modified or eliminated by changes in Federal or state law, and the laws regarding eligibility may change before you apply for MA benefits.
- Nursing homes can be "de-certified" as MA-participating nursing homes. If this de-certification happens, nursing home residents may need to move to a certified nursing home to continue receiving MA benefits.
- If the property is titled in the names of several people, transferring title to the property becomes more cumbersome, and may be a source of conflict between them.
- Assets placed in the names of others may be subject to creditors' claims if the property owners experience credit problems. These creditors may include an ex-spouse as part of a divorce proceeding.
- Liquidating some assets to facilitate the transfer may cause the imposition of some penalties for early withdrawal, depending on the terms of the investment.
- Placing assets in a son's or daughter's name may mean that son or daughter will receive that property after the original property owner's death, which may upset an estate plan of trying to divide the property equally among one's children.

ESTATE TAX CHANGES

The Economic Growth and Tax Relief Reconciliation Act of 2001 brought substantial changes that affected estate

planning in a number of ways. Among other changes, that law increased the amount a person could own without paying estate taxes (the "Unified Credit"), reduced the maximum estate tax rate, and repealed the estate tax for deaths occurring in 2010. However, there was a quirk in the law. A "sunset" provision included in the law would bring back the estate tax if Congress took no action prior to 2011.

Acting at the 11th hour, Congress passed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "Tax Relief Act") in December, 2010. Amongst other changes, including the extension of the Bush-era income tax cuts, the Tax Relief Act gave estates for deaths occurring in 2010 the option of electing between being exempt from the estate tax with limited adjustment in tax basis of assets, or being subject to estate tax with a higher exclusion amount or Unified Credit, lower estate tax rates, and a greater adjustment in tax basis. The Tax Relief Act increased the Unified Credit to \$5 million for deaths occurring in 2011 and 2012; lowered the estate tax rate to 35%; and "sunset" these changes on December 31, 2012, unless Congress acts to extend the changes before then.

In General

When contemplating estate planning and avoidance of what is commonly referred to as the "Death Tax", there are a number of basic concepts that a person must first understand. Understanding the "Unified Credit", "Basis" and the "Annual Gift Tax Exclusion" and their effects on the Death Tax are essential before a person can begin planning.

The "Unified Credit", in its simplest terms, represents the total amount of value of assets and the total of all lifetime taxable gifts a person can make before the Internal Revenue Service (IRS) is going to begin taxing the assets a person owns when they die. "Basis" is a dollar amount every piece of property has which the IRS uses to determine income tax consequences when ownership of that piece of property is

transferred. The "Annual Gift Tax Exclusion", which you may have seen referred to as the Section 2503 tax exclusion, represents one of the most basic tax saving devices available under the tax code. In any year, a person can give up to \$13,000 to any other person with absolutely no gift or estate tax consequences. These three basic aspects of estate and gift tax work with and have various effects on one another.

The Unified Credit

The Unified Credit currently stands at \$5,000,000. It should be noted, however, that upon the death of the first spouse, an unlimited amount of assets can be transferred to the surviving spouse without estate tax liability. The Tax Relief Act also made the unused portion of the Unified Credit "portable" between spouses, meaning that the surviving spouse could have an estate worth up to \$10 million without paying estate taxes.

Under the Tax Relief Act, the Unified Credit is as follows for decedents dying, and gifts made during the listed years:

Unified Credit	Exclusion
2010	\$5,000,000.00 ¹
2011	\$5,000,000.00
2012	\$5,000,000.00
2013	\$1,000,000.00 ²

Even though estate taxes only apply to the portion of estates greater than these amounts, estate tax planning is still important. Remember that if Congress fails to take any action after 2012 the estate tax exemption, or Unified Credit, will revert to \$1,000,000. Without careful planning there may be income tax problems related to estate taxes payable or a decrease in the amount of property subject to the step-up in basis.

Estate Tax Rates

¹ Estates of decedents dying in 2010 may elect to be exempt from the Death Tax and receive only limited adjustment in Basis.

² Unless Congress acts before then, the Unified Credit will revert to \$1 million in 2013.

The Tax Relief Act set the highest estate tax rate at 35% of those estates worth more than the Unified Credit amount (\$5 million in 2011 and 2012, potentially reverting to \$1 million in 2013).

Similarly, if Congress fails to act before 2013, the top estate tax rate will revert to 55% (or potentially more) of those estates worth more than the Unified Credit amount. Because of the significant tax rate that may apply to estates worth more than the Unified Credit amount, planning to minimize or avoid estate taxes can be an important planning priority.

Basis Adjustment

In General:

The Basis of a piece of property determines the amount of tax a person will pay when that piece of property is sold or transferred in some way. If a person purchases a parcel of farmland for \$5,000 in 1950, the Basis of the land is the cost - (\$5,000). Now say that over 40 years the farmland increases in value to \$250,000. The value has increased, but the Basis remains the same. If the person were to have sold the land in 1990 they would have been taxed as follows:

Land Sale Price =	\$250,000
Land Basis =	<u>\$ 5,000</u>
Amount Subject to	
Income Tax =	\$245,000

This is not a very appealing situation. The parcel of land has become what tax professionals call an "appreciated asset."

Step-up In Basis:

Now suppose the owner of the land (still valued at \$250,000) keeps the land until they die at which time they leave the land in their Will to a child.

Because the land is transferred to a person from another person's estate it is exposed to potential estate tax and receives a new Basis which is the date-of-death fair market value of \$250,000. This is what tax professionals commonly refer to as a "step-up basis" or an "adjusted basis." If the child

immediately sells the land for \$250,000, the calculation of the amount of gain subject to income tax on the sale is as follows:

Land Sale Price =	\$250,000
Land New Basis =	<u>\$250,000</u>
Amount Subject to	
Income Tax =	\$ 0

Based on a tax rate of 25%, the "step-up in basis" saves up to \$61,250 in income tax liability. This "step-up" in Basis is the reason many people keep appreciated assets in their estate and transfer them to family or friends at their death.

GIFT TAX MATTERS

Annual Gift Tax Exclusion

In 2011, you can give up to \$13,000 per year to another individual without negative tax consequences. A married couple can give \$26,000 (\$13,000 from each spouse). There is no tax limit on how many people to whom you can give up to \$13,000. If you have 10 people to whom you would like to give \$13,000, you can give them each \$13,000 for a total of \$130,000 gifted in one year with no gift or estate tax consequences. Generally, it is best to give assets with a high tax Basis and keep assets with a low tax Basis. While gifts of less than the exclusion amount may not have tax consequences, those gifts may have consequences in other areas, such as Medical Assistance eligibility, as discussed elsewhere in this newsletter.

Gifts of more than \$13,000 to one person in any calendar year must be reported on a gift tax return, which must be filed no later than April 15 of the year following the year in which the gifts were made. Even though a gift tax return must be filed, unless the donor's lifetime gifts reported on all gift tax returns exceed \$5 million, no gift tax will be due or payable. A gift reported on a gift tax return does, however, reduce the amount of the Unified Credit that will be used in calculating the donor's estate tax upon their death and it will reduce the Unified Credit amount by a dollar-for-dollar amount.

To determine the true value of assets reported on a gift tax return, those assets may need to be appraised. The IRS is not required to accept the appraiser's opinion. Also, a gift results in no "stepped-up" Basis. In other words, the donor's Basis in the property would transfer along with the asset to the person who receives the gift.

Income Tax Treatment of Gifts

Gifts are not taxed or reported as income to the recipients and similarly are not deductible by the donor. If the gift is property, like real estate, the recipient may have taxable income if and when the recipient sells the gifted item.

FUTURE ESTATE TAX PLANNING

Because of the uncertainty of the future of the Unified Credit amount, it is a good idea to plan for the "worst case scenario" (that is, the lower Unified Credit amount of \$1 million). Some options to consider if you are concerned that the size of your estate will make it subject to the estate tax:

- Make gifts of less than the Annual Exclusion Amount to reduce the size of your estate to less than the Unified Credit amount.
- Include bequests to charities in your Will to reduce the value of your taxable estate to less than the Unified Credit amount.
- Include a "disclaimer trust" in your Will to allow a surviving spouse to "disclaim" a portion of your estate into a separate trust that will pass outside of the surviving spouse's estate upon his or her death.

It is a good idea to review your Will and other estate planning documents at least annually. In this way, you can modify your estate planning documents to reflect changes in your personal situation (e.g., whether your children may need a guardian, who you would like to serve as the personal representative in your estate) and for changes in the law. You can also modify the distribution of your assets in the manner you want.

USEFUL INFORMATION FOR ESTATE PLANNING

The death of a loved one can cause anguish, uncertainty, and stress, especially for a surviving spouse. For these reasons, it is helpful to the survivors to organize in one location information about your assets during your lifetime. Doing so can reduce the headaches that accompany the heartache. Here is information you should gather:

- List of all real estate owned, including copies of deeds and real estate tax statements.
- List of all bank accounts, including name and contact information of financial institution, account number, current P.O.D. beneficiaries (if any), and a copy of a recent statement.
- List of all stocks, including company or fund name, broker name and contact information, account number, and a copy of a recent statement.
- List of all life insurance policies, including company name, agent name and contact information, policy number, current beneficiaries, a copy of a recent statement, and a copy of the policy.
- List of all annuity contracts, including company name, contact information, contract number, current beneficiaries, a copy of a recent statement, and a copy of the contract.
- List of all safe deposit boxes, including name of financial institution, contact information, box number, and description of location of key.
- List of all vehicles, including make, model, year, vehicle identification number, and location of title.
- A description of the location of your original Will.

For security reasons, it is a good idea not to store all of this information on your computer hard drive. You may want to maintain it in written format and be sure the people nominated to serve as your personal representative under your Will know where they can find it.

Gathering this information in one location can also make meeting with an attorney to assist with your estate planning more efficient and productive.

Please remember that this Newsletter is only a general discussion of the law and some estate planning concepts. When planning for your estate, it is always important for you and anyone who assists to be sure that your estate plan is the right plan for you and that it meets your wishes and desires. If you would like to discuss your estate plan, please call our office to set-up an appointment.

ABOUT OUR FIRM

Kostner, Koslo & Brovold LLC offers all clients a full range of income tax as well as gift and estate tax planning and preparation services.

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