

BLOISE & SNAVELY LAW OFFICE

NEWSLETTER

283 South Hamilton St.
Painted Post, NY 14870

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MAXIMIZE YOUR GIVING, REDUCE YOUR TAXES

In a recent issue of Bottom Line's Tax Hotline, Attorney and Professor of Law, Christopher R. Hoyt, describes a common trap for those who have substantial retirement savings. The money in your retirement plan accounts may be most of your life savings, but it also may be taxed at rates of 64% or more when you die, due to the double-tax effect of combined income and estate taxes. You need to know how to leave less of these monies to the IRS and more to your heirs.

Funds held in a qualified retirement plan, like an IRA, 401(k) or 403(b), are subject to death tax when you die, just like all other assets you own. [Death tax can be the New York and Federal estate tax, as well as the

Pennsylvania inheritance tax]. The same funds are subject to income tax when distributed from a retirement account or traditional IRA to an account beneficiary.

Federal estate tax currently applies to estates greater than \$2,000,000, but this amount is scheduled to decline to \$1,000,000 in 2011. The applicable rate is 45%. Income tax applies to retirement plan distributions at rates up to 35%. Combine the estate and income tax rates and the effective tax rate can reach 64%.

For example, in 2011 a retirement plan account has a balance of \$100,000 and is included in the estate of a decedent whose other assets total \$1,000,000. The retirement account balance will be distributed in the year of death to a beneficiary in the 35% income tax bracket. The estate will owe \$45,000 of estate tax on the account and the beneficiary will have \$100,000 of taxable income from the distribution. The

beneficiary does get some benefit through an income tax deduction for the estate tax paid, but he still will owe an extra \$19,250 in income taxes.

The combination of \$45,000 of estate tax plus \$19,250 of income tax equals \$64,250 – a tax rate of more than 64% - and leaves just \$35,750 left from the original \$100,000. Even worse, the total tax bill will be even larger for New York and Pennsylvania residents because of state death and income taxes. These state taxes can push the combined federal and state tax rate to more than 80%.

What can you do? Here are some suggestions Professor Hoyt makes to avoid the double taxation of retirement savings that you leave to your heirs. **First**, make charitable gifts. If your estate is going to owe estate tax and you intend to make charitable bequests, state in your will or trust that the bequests are to be funded using your retirement accounts instead of other assets. When received by a charity, such funds escape income tax and estate tax. The taxes saved on such a bequest can let you leave more to your heirs.

Second, avoid saving too much in retirement accounts. Once you have sufficient funds in retirement accounts to meet your retirement needs, place additional savings in

other types of investments. For example, life insurance proceeds are free of income tax and, with proper planning, can be estate tax free also. Thus, your insurance premiums can provide a bequest to heirs that is double tax *free* (i.e., no estate or income tax) instead of double taxed. This is perhaps the best use of life insurance you may ever see, but professional help is necessary.

Third, withdraw excess funds from retirement accounts. Take distributions from retirement accounts and use them to buy investments such as life insurance or appreciating capital gain assets that will be income tax free to heirs.

Fourth, minimize your estate. Reduce the size of your taxable estate by making the maximum annual gift exclusion of \$12,000 per person. These gifts will move assets out of your estate to heirs free of gift and estate tax while you are alive.

Fifth, combine the third and fourth recommendations so that the annual gift amount is being used to purchase life insurance inside a life insurance trust. This strategy both minimizes your estate and gives your heirs an inheritance that is income and estate tax free. ■

Giving More

For those inclined to give more to charity, you can use the same ideas mentioned in the previous article to give more to your favorite nonprofit organization. If you have an annual practice of giving to certain charities, why not continue that practice for 10 or 20 years after you or you and your spouse are gone? A life insurance trust protects against premature death by guaranteeing that your giving will not stop. The trust also protects the future stream of donations by protecting the policy from your creditors and the organization's creditors.

FREQUENTLY ASKED QUESTIONS the girls in the office receive:

1. DO YOU HAVE MY ORIGINAL DOCUMENTS IN YOUR OFFICE?

Generally, the only "original" documents we keep in our office are Last Wills done after October 2003.

Because space is limited we can not keep everyone's originals here.

Typically, at the time you signed your documents, your

originals were given to you. If you did a will plan, your originals should be in a gray or blue folder. If you did a trust plan, your originals should be in a large brown envelope.

2. DO YOU STILL HAVE A MANSFIELD, PA OFFICE?

No. We moved our office to Painted Post, New York in 2003, but Attorney Snavelly is still licensed in PA, works with new PA clients and continues to service his current PA clients.

3. WHAT IS THE TAX ID # FOR MY TRUST?

The tax identification number for a Revocable Living Trust would be, for a married couple, the husband's Social Security number, and for singles, their own Social Security number.

4. CAN YOU GIVE ME A QUICK EXPLANATION OF A MEDICAID TRUST?

No. There is no "quick" answer. Only Attorney Snavelly is qualified to answer questions regarding Medicaid issues. The girls would be glad to set an appointment for you though!

DIRECTIONS

From North, East and West of Corning/Painted Post area:

Take exit 44 off of Route 86 (old Route 17)

Follow signs for 15 South

Take Exit 3 (417, Gang Mills)

At the traffic light, turn right (417 East)

We are on the right hand side about 0.7 mile, in a plaza of shops.

From South of Corning/Painted Post area:

Take 15 North

Take Exit 3 (417, Gang Mills)

At the traffic light, turn left (417 East)

We are on the right hand side about 0.7 mile, in a plaza of shops.

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Sign up today for our electronic newsletter. Simply email us at snavelylaw@yahoo.com and request to receive our next newsletter via email.

“Helping people pass on assets to their families and, at the same time, avoid death taxes, probate and nursing home costs”