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Financial Planning Strategies

A Financial Planning Update

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An Alternative for Maximizing the Applicable Exclusion Amount

One of the most common estate planning strategies for married individuals is for each spouse to leave his or her entire estate to the surviving spouse. Due to the **unlimited marital deduction**, an entire estate (regardless of size) can pass to the surviving spouse without incurring any federal estate taxes upon the first death. However, such a strategy fails to take advantage of the **applicable exclusion amount** of $2,000,000 for 2006* that *each individual* can transfer to heirs completely free of gift or estate taxes, potentially subjecting the survivor's estate to higher than necessary future taxes. This undesirable situation occurs because *all* property remaining in the survivor's estate will otherwise be subject to estate taxation.

One popular trust arrangement designed to address this issue *in advance* is the common "**A/B**" combination, typically set up as a **revocable trust** that can be modified at any time prior to death. However, there is another option, known as a **qualified disclaimer** that can provide some flexibility *after* a spouse has died.

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Review Your Credit Report for Identity Theft Protection

Identity theft is a serious crime to the American consumer, with over 255,000 individuals affected in 2005 alone (The Federal Trade Commission (FTC), 2006). As one part of a protection strategy, the FTC and other consumer credit organizations suggest a proactive approach to safeguarding your identity: monitoring your **credit report**. A credit report is an accumulation of information about your bills and loans, your repayment history, your available credit, and your outstanding debts. These reports are typically used by lenders when deciding whether or not to accept a loan or credit application. In terms of identity theft, your credit report can alert you to accounts that have been fraudulently opened in your name, unauthorized charges made to your existing accounts, and other crimes committed by someone using your personal information.

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An Alternative for Maximizing the Applicable Exclusion Amount

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More about Qualified Disclaimers

This postmortem planning technique may be useful in situations where "A/B" trusts or similar arrangements were not established prior to death. Rather than transfer all property to the surviving spouse using the unlimited marital deduction, thereby wasting the first spouse's applicable exclusion amount, the surviving spouse can disclaim a portion of his or her inherited property. The disclaimed property then passes to other heirs or beneficiaries as if the surviving spouse had predeceased. The estate can then take advantage of the applicable exclusion amount with respect to the disclaimed property.

In order to be effective for federal tax purposes, a disclaimer must meet the following requirements:

- The disclaimer must be in writing and be irrevocable.
- The disclaimed interest must pass without direction by the person disclaiming the property. Consequently, before deciding to disclaim, it is advisable to know who, under the will or applicable state laws, will receive the property instead. Typically, a will can direct the disposition of any disclaimed property.
- The written refusal must be received by the grantor of the interest (or the grantor's estate) within nine months of the taxable transfer creating the interest (or, where the disclaimant is a minor, within nine months of the disclaimant's 21st birthday).
- With the *exception* of a spouse, the person disclaiming the property cannot receive any benefit from the disclaimed property, such as trust income.

Spouse's Special Exemption

If the surviving spouse wants to take advantage of this strategy, yet desires a lifetime income from the disclaimed property, a provision in the decedent's will could accomplish this feat by establishing a **disclaimer trust**. With this alternative, the surviving spouse can effectively establish an "A/B" trust *after* the death of the first spouse.

Disclaiming an inheritance might prove useful in certain situations. For example, suppose your wealthy uncle, a widower without children, has named you as the beneficiary of his entire estate. However, he has also stipulated that should you die before him, his estate will be distributed to your children. Sadly, your uncle passes away unexpectedly, at a time when you are financially comfortable and really don't need the money. Accepting your inheritance will just increase the value of your estate and, hence, your potential tax bill when it ultimately passes to your children. A better alternative might be to benefit your children *today* by disclaiming the inheritance, with no associated gift tax imposed as a result of the transfer, assuming all qualified disclaimer requirements are satisfied.

Proceed with Caution

Be aware that there are instances, such as in smaller-sized estates for which a surviving spouse's standard of living will be dependent upon all of his or her assets, where a qualified disclaimer may not be an appropriate choice. In addition, if the property in question is of substantial value and is transferred to an individual two or more generations younger than the donor, a disclaimer could trigger **generation-skipping transfer (GST) taxes**.

Nevertheless, under the appropriate circumstances, a qualified disclaimer may be an effective tool to assist in reducing the effects of transfer taxes. Remember, however, that any decision to disclaim an inheritance should be reviewed carefully, in advance, with a qualified legal professional to determine if such a decision is consistent with your overall goals and objectives. $

** The applicable exclusion amount is scheduled to gradually increase to $3.5 million in 2009. Unless Congress enacts further reform, federal estate taxes will be repealed in 2010, and then reinstated in 2011 at levels in effect prior to the Economic Growth and Tax Relief Reconciliation Act of 2001.*

Retirement—A Community Audition

A house once filled with the constant, clamoring sounds of a growing family has grown silent. Family visits have become few and far between. The silence seems deafening. If these thoughts seem familiar, maybe you and your spouse have outgrown a home you once considered to be too small.

Although our specific housing needs change as we age, shelter, in any form, is always much more than mere physical comfort. It is a financial, psychological, and social base, which anchors our sense of stability. For this reason, it is common to find people who had moved to warmer climates in their early retirement years later returning to the familiarity of their original communities and the proximity of family and friends.

With many other soon-to-be seniors finding themselves in similar situations, **retirement communities**, also known as **55+ communities**, have become a possible alternative for people looking to downsize their homes. These neighborhoods or complexes, which vary from condominium-style settings to single family homes, usually require that at least one member of the household be age 55 or older.

Retirement communities typically offer an active and independent lifestyle to those who do not require **assisted living facilities (ALFs)**. The Housing for Older Persons Act of 1995 eliminated the requirement that these communities have "significant facilities and services designed to meet the physical and social needs of older persons." This legislation has increased the popularity of such communities as an alternative for people age 55 and over, who do not require assistive care.

Considerations

Relocation, of any kind, requires a careful examination of the possible pros and cons. Before selling your home to move to the newest 55+ community, consider the following:

Security. Retirement communities may offer security that a typical neighborhood would not. Generally, they have security guards at the entrance of the neighborhood or building. Knowing this added protection exists, you may sleep more soundly at night.

Recreation. With people living longer than ever before, gone are the days when retirement brings to mind an idle existence. These days, retirement can be as active and as fun as you make it. Generally, retirement communities offer a recreation center that manages group activities that may be as vigorous as sporting events, or as leisurely as card games.

Medical Facilities. Many retirement communities have medical facilities located within the property limits. You or your spouse may not require constant care; however, it can be comforting to know that qualified medical professionals are accessible at any time.

Maintenance. Although you might have once considered shoveling snow, mowing the lawn, and picking weeds pleasurable pastimes, they may now be tiresome. Oftentimes, these self-contained neighborhoods handle exterior maintenance—including lawn care and snow removal. A retirement community enables you to enjoy a yard without having to maintain it.

Costs. The services retirement communities provide come at costs that must be considered in addition to typical homeowners' expenses. Usually, there are entrance fees and monthly maintenance costs (similar to condo fees), which may increase your purchase price by thousands of dollars.

Limited Socialization. While many people consider a retirement community's socially-oriented lifestyle an advantage, some consider it a disadvantage. If transportation is not readily available, the prospect of frequently being surrounded by the same group of people could seem confining.

Determining where you want to spend your "golden years" is a decision that requires serious consideration. However, whether you choose to stay in your current situation, decide to call a retirement community home, or opt to explore other living arrangements, it is important that *you* are comfortable with your choice. $

Review Your Credit Report for Identity Theft Protection

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According to the **Fair Credit Reporting Act (FCRA)**, you can request a free copy of your credit report from each of the three major credit bureaus (Equifax, Experian, and TransUnion) once a year. For your convenience, you can access all three agencies through a single website, www.annualcreditreport.com. The FTC suggests that you order all three reports, even if you choose to stagger your report requests throughout the calendar year, as the information contained within may not be the same from each bureau. This happens because credit reporting is done on a voluntary basis: Creditors may subscribe and report information to just one agency or all three.

Reviewing Your Reports

Typically, a credit report is divided into four major sections: identifying information, credit history, public records, and inquiries.

The **identifying information** on your report will include your name, current (and previous) address, Social Security number, driver's license number, telephone number, birth date, current and previous employers, and your spouse's name, if applicable.

The **credit history** section details your payment history with banks, retail stores, finance companies, mortgage companies, and others who have given you credit. It is in this section where accounts opened or affected by identity thieves may become apparent. Each account, sometimes called a trade line, will appear with the following information: name of creditor, account number, type of credit (i.e., installment loan or revolving credit), account participation (e.g., joint owner, individual account, or authorized user), date opened, last activity (date of last payment or charge), high credit (the credit limit or original loan amount), terms (number of installments or amount of monthly payments), balance at the time of reporting, past due balance at the time of reporting, status of the account (open, closed, inactive, etc.), and date of last report.

The **public records** section includes public records that reflect your history of meeting financial obligations, such as bankruptcies, collection accounts, judgments, and tax liens. Since records applicable to this section have a serious, negative affect on your credit, ensure that the information belongs to you, not someone who falsely used your personal information.

Finally, the **inquiry** section lists all the businesses that have received your credit report during the last 24 months. Inquiries are categorized as hard or soft. Hard inquires are those you initiate by filing a credit or loan application. Soft inquiries often come from marketers who want to sell you something. If a listed business sounds unfamiliar, be sure to find out the nature of the business and why they are looking at your credit report.

Mistake or Identity Theft?

If you find a mistake on your credit report, it is important to contact the credit bureau that issued the report, using the form provided with the report or following the instructions given by that particular agency. If the error is more serious, and you suspect your identity has been stolen, contact the FTC's Identity Theft Hotline at 1-877-IDTHEFT (877-438-4338). Be sure to keep thorough documentation of all communications with creditors, agencies, and the FTC.

For more information about steps to take if you become a victim of identity theft, visit the FTC's website at www.ftc.gov. $

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