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Executive Compensation ■ Succession ■ Wealth Transfer Planning

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Alphabet Soup: ILITs and the GST

With Federal estate taxes designed to tax assets transferred from one estate to another, planning to preserve wealth for your children, grandchildren, and future generations can be challenging. In 2017, the Federal estate and gift tax rates are as high as 40%; therefore, wealthy individuals, as well as those of modest means, need to carefully formulate their financial and estate plans in order to help *minimize* taxes and *maximize* their financial legacies. As a result, the **irrevocable life insurance trust (ILIT)** has become recognized as a straightforward mechanism for funding future estate tax liabilities and creating the potential for leveraged gifts to family or charity. However, in such cases, estate planners should also be aware of the implications of **generation-skipping transfer (GST) taxes** and take special care to ensure this additional transfer tax is not incurred.

Annual gifts by a donor to an ILIT are typically used to make premium payments on a life insurance policy insuring the life of the donor(s). The size of the gift will determine the amount of insurance the ILIT will be able to purchase. Thus, it is not uncommon for grandchildren to be included as ILIT beneficiaries in order to maximize the use of the donor's **annual gift exclusion** ($14,000 annually per donee and $28,000 for gifts made by a married couple) and Crummey withdrawal powers.[1] The proceeds of a properly executed ILIT will not be included in the estate of the donor(s).

The GST tax is an additional tax imposed on all transfers (during one's lifetime or at death), either outright or in trust, to a skip person, when the transferred assets are not subject to gift or estate taxes in the gross estate of the skipped generation. A skip person is an individual at least two generations removed from the generation of the transferor. For example, if a grandparent is a transferor, a grandchild qualifies as a skip person. The GST tax rate is currently equal to the maximum 40% Federal estate tax rate and is applied to the entire transferred amount. However, every individual has a **generation-skipping exemption** ($5.49 million in 2017) for transfers while living, as well as those at death; the generation-skipping exemption cannot be transferred between spouses.

It should be noted that the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) has amended the GST tax exemption amount in any calendar year to equal the estate tax applicable exclusion amount in effect for that calendar year.

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Perk Up Your Employees—They May Feel Better

Employers are looking for more ways to promote employee productivity and provide incentives for working toward company growth. As an employer, you may spend a lot of time focusing on salary, benefit plans, a positive work environment, and vacation schedules to perk up your employees. However, you may want to motivate your workforce by offering a menu of fringe benefits that can make a significant difference in the workplace environment and employee morale.

Here are five options that you may want to consider:

1. Qualified transportation fringes. Travel expenses can really add up, especially in heavily congested urban areas. Your employees may live near a transit line and commute to work, or they may drive to work and pay for parking. As an employer, you can provide cash reimbursement to your employees for transportation and parking, and your employees can exclude the payments from their gross income. Through 2017, the amount that may be excluded for qualified mass transit, van pools, and parking is $255 per month.

2. Working condition fringes. Not all fringes involve reimbursements or advances. Suppose your company sells products or provides services that require significant automobile travel. As a perk, you can provide a company vehicle (even with a driver) for business use. Consequently, your employee's car is spared the wear and tear. In addition, you can pay for an employee's business travel by airplane or train. Another fringe may be to offer employees the opportunity to work from home, when possible.

3. No-additional-cost services. If your business offers services to customers, you may be able to offer those same services to your employees. As long as there is no loss of income or additional cost to your business, you may offer the services to your employees free of charge. For example, an airline may offer a flight attendant the perk of flying for free on a "standby" basis. The flight is at no cost, and the employee is flying in an otherwise vacant seat. These types of fringe benefits may also apply to certain employees of hotels, cruise ships, and communication companies.

4. Qualified employee discount. For businesses that sell products or provide services to customers, why not provide an employee discount? If you sell a product, your employee discount would be the current sale price multiplied by your "gross profit percentage." If your business provides services, the maximum discount is limited to 20% of the current price for services offered to your customers.

5. De minimis fringes. Even some smaller perks may boost employee morale, reinforce productivity, or recognize special occasions. For instance, you may provide tickets to a theatre or sporting event, organize a dinner at a restaurant, or give out flowers or fruit baskets for outstanding service, employee illness, or family crisis. Your employees may appreciate your thoughtful gestures, as well as the positive recognition or compassion you have taken the time to express.

Smaller fringes may also involve occasional perks *within* the workplace. For example, if you ask an employee to work overtime, you may provide money for meals and local transportation fare. Be creative and come up with other perks that your employees may appreciate.

Fringe benefits can play an important role in creating a positive work environment. They can help create a bond between you and your employees and increase employee loyalty. Would one or more of these fringes be appropriate for *your* business? A thorough review can help you find out. ■

It's Time to Conduct an Inventory

Try closing your eyes and listing your living room furnishings or the contents of your jewelry box. If you have trouble coming up with a complete tally, imagine how hard it would be after the stress of a fire or burglary.

Making a written inventory of your household valuables can be one of the best money-saving steps you can take. Property insurers are less likely to question claims based on such inventories, particularly if you submit photographs, videotape, receipts, or an appraiser's statement for valuable items. Your insurance company may even be able to give you a useful inventory form to fill out. Make sure to keep a copy of your inventory of household valuables with your insurance agent or in your safety-deposit box.

For the Record

Write down the date you purchased each item of value in your home, including its price. If an appraiser has estimated the value of any of your possessions, record the estimate and the date of the appraisal, making sure the appraisal is precise and explicit.

Describe each object in as much detail as possible. Be sure to include its age, brand name, size, model number, and other relevant facts. For example, for sterling silver tableware, note the manufacturer, pattern, and number of place settings. If your possessions are extensive and of particularly high quality, you may also consider videotaping and recording your verbal description of them.

In some categories of property, such as clothing, you may wish to group together a number of articles and attach a single estimate of value. Unless you have closets filled with designer originals, there may be no reason to complicate matters by describing everything in your wardrobe.

Remember, of all the ways to record your property, the worst one is memory. Because, if you don't remember you own it, neither will your insurance company. ■

alphabet soup: ILITs and the GST

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Dotting the I's and Crossing the T's

When properly drafted and implemented, an ILIT can be a creative tool for passing wealth to future generations while avoiding GST taxes. In many instances, this can be achieved without using the donor's generation-skipping exemption. Nontaxable gifts, such as those made under the annual gift exclusion, are excluded from the GST tax.[2] However, when nontaxable gifts are made to a trust, two additional vesting requirements must be met for the trust to be exempt from GST taxes.[3] First, the distribution of trust income and principal must be limited solely to the trust beneficiaries. Second, if a beneficiary predeceases the life of the trust, the deceased beneficiary's interest in the trust must be includable in his or her gross estate.

The use of ILITs is fairly commonplace in today's estate planning arena. However, the importance of the GST tax is typically underestimated. Thus, great care should be taken to help ensure that GST taxes do not undermine the benefits of an ILIT. ■

[1] Crummey v. Comm., 397 F.2d 82 (9th Cir. 1968).
[2] IRC Sec. 2642(c)(3).
[3] IRC Secs. 2642(c)(2) and 2652(c)(3).

Financial Challenges for the "Sandwich" Generation

Given the fast pace of life, many parents struggle to keep up with their family and career obligations. It's easy to feel caught in a tug-of-war, pulled in multiple directions by family responsibilities and day-to-day demands of a career. Working Baby Boomers in particular, who are "sandwiched" between obligations to their children and their aging parents, often feel like they're juggling three full-time jobs. Sound familiar?

The financial responsibilities involved are many: investing time in your career; paying for a child's education or accommodating a special needs child; funding or providing care for an aging parent; and saving for your own retirement.

How can you make it all work without feeling torn between competing priorities? In every area of your life, planning can help you develop strategies to optimize your time and financial resources to achieve your goals.

Raising Children

Parents want the best for their children, and education is often essential to success. But with sky-rocketing tuition costs, college can seem unattainable. However, there are several options: scholarships, loans, grants, and financial aid. To enhance your college funding plan, start saving what you can as early as possible. You might be surprised at what you can accomplish with a disciplined approach to saving over time. In addition, there are Federal tax credits and tax-efficient savings vehicles tailored specifically for education, including prepaid tuition programs, college savings plans, and Coverdell Education Savings Accounts (ESAs).

Caring for Aging Parents

While raising families and cultivating careers, parents are often called on to care for their own aging parents, relatives, and spouses. At some point, this may become a reality for you whereby you face time constraints and the increased financial burden of caregiving. Since many people can't afford to put their work on hold to be a caregiver or to pay for extended care out of pocket, long-term care insurance (LTC) may help to alleviate these concerns for you and your loved ones.

With many LTC policies helping with coverage of care at home, as well as in assisted living facilities or nursing homes, you may want to consider LTC insurance as an important component of your retirement planning. Having LTC insurance in place may help to avoid family caregiving burdens on the next generation. LTC insurance may also help you preserve assets and meet your estate planning goals, such as leaving a legacy for children and grandchildren. As with most types of insurance, it is cost-effective to obtain coverage *before* you or a loved one needs it.

You First

Parents often put the needs of others before their own. But, unlike the assistance available for college, there are no loans or financial aid for retirement. Since retirement funds typically come from three main resources: Social Security, company-sponsored retirement plans, and personal savings for many people, it's important to save what you can, when you can. Contribute to your company's retirement plan and maximize your contributions for the company match, if available. If your company does not offer a retirement plan, open an Individual Retirement Account (IRA). In addition, plan for the unexpected. Disability income insurance can help replace a portion of your income in the event of an accident or illness, and life insurance can provide a benefit for your family in the event of your death.

Looking Ahead

With sound planning and the professional guidance of a qualified financial professional, you may be able to minimize the emotional and financial stress of family obligations, and tailor a long-term plan to meet your future goals. ■

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