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**Treasury
Department
Revises Rules for
IRAs**

CARL ROSEN

In 2001, the Treasury Department substantially revised and simplified the rules governing the required minimum distributions from IRAs and qualified retirement plans (the minimum distribution rules determine when distributions must begin and the minimum amount that must be distributed each year). The following is a summary of the new rules:

● **Generally, you cannot take distributions from your IRA before age 59½** without incurring a 10

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COVER STORY

**New Automatic Rules for
Irrevocable Trusts
Explained**

NATHAN TOWNSEND

Do you have an insurance trust or an irrevocable trust that was created for gifting assets? If so, you need to know about the new rules, so that you can be sure that your generation skipping transfer (GST) tax exemption is not exhausted without your knowledge.

The 2001 Tax Relief Act, which was signed into law on June 7, 2001, modifies the rules for allocating GST exemption to transfers that are made to irrevocable trusts.

In the past, relatively few transfers in trust would result in the automatic allocation of GST exemption. Most often one's GST exemption was applied to transfers by the allocation by a taxpayer upon the filing of a gift tax return. Under the new law, transfers to irrevocable trusts are more likely to result in automatic allocation of GST exemption. Taxpayers have an opportunity to elect not to

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SPOTLIGHT:

529 Plans Make Saving For College Easier

MICHAEL A. DRIBIN

Learning the basics, restrictions and benefits of 529 Plans

What was already an attractive way to set aside funds for higher educational expenses has become a great way to accomplish that goal as a result of the Economic Growth and Tax Relief Reconciliation Act of 2001.

The Basics

A donor may contribute to a 529 Plan on behalf of the designated beneficiary (most often, a child or grandchild). To the extent permitted under the Plan, amounts saved in a 529 Plan may be used for the higher educational expenses of the designated beneficiary. The

panies administer the plans. The donor invests assets in a specified portfolio of mutual funds, or in a portfolio of mutual funds tailored to the age of the designated beneficiary. The donor retains complete control and may even change the designated beneficiaries. Some Plans allow investment in the 529 Plans by assets held in account under the Uniform Transfer to Minors Act.

Restrictions

Contributions to a 529 Plan are made with after-tax dollars and qualify for the gift tax annual



while in the account. When one pays educational expenses from the account, the distributions are not considered income to the beneficiary. If distributions are made from the account to pay for things other than education expenses, they are subject to income tax by the beneficiary and a 10 percent penalty.

THESE PLANS OFFER AN OUTSTANDING OPPORTUNITY TO PROVIDE FOR COLLEGE EDUCATION, WITH TREMENDOUS TAX SAVINGS.

designated beneficiary must be enrolled in an “eligible educational institution” — any institution whose students are eligible to receive federal student financial assistance.

The 529 Plans are sponsored by individual states. However, at the present time, 30 of these plans are open to residents of any state.

Major money management com-

panies administer the plans. The donor may contribute up to \$55,000 per designated beneficiary in one year and elect to spread the contribution over five years for annual exclusion purposes. A gift tax return needs to be filed if this is done. Contributions are prohibited in excess of what is necessary to pay for qualified higher educational expenses.

The funds grow income tax-free

The Benefits

529 Plans provide a great opportunity to fund college educational expenses for children or grandchildren, with no income tax consequences to anyone. The gifts — to the extent of \$11,000 per year (or \$55,000 if made in one payment for one beneficiary) — are excluded from any gift tax considerations. These plans offer an outstanding opportunity to provide for college education, with tremendous tax savings. **BC**

This article is a brief summary of 529 Plans. Anyone considering creating such a Plan should consult his or her tax advisor or Broad and Cassel's Estate Planning offices.

IRREVOCABLE*continued from cover*

allocate their GST exemptions by filing a gift tax return for the year in which the contribution was made to the trust.

Your most important tool to minimize or eliminate the GST tax (applied currently at a flat 50 percent) is the GST exemption. This exemption currently allows each taxpayer to transfer just over \$1 million during lifetime or at death — without subjecting the transferred assets to the GST tax. Unfortunately, under the new tax law, you risk inadvertently depleting your GST exemption simply by making transfers to irrevocable trusts.

As the use of one's GST exemption is an integral part of a complete estate plan, it's important not to allow such inadvertent application of this valuable exemption. The only certain way to ensure you are properly planning for the most effective use of your GST exemption is to file a gift tax return for each year in which contributions are made to your irrevocable trust. On that return, you will either elect to allocate GST exemption to the transfers made to the trust, or you will elect not to allocate the GST exemption to these transfers. **BC**

If you have created one of these trusts, take control of the allocation of this important exemption, rather than allow the IRS to dictate when it is allocated. In light of these new laws, if you are unsure if this new allocation rule applies to you, we would be happy to discuss this and any other estate planning issues with you.

TREASURY *continued from cover*

percent penalty, and distributions must start by your required beginning date, which is April 1st of the calendar year after you reach age 70½.

- **Prior to the change, IRA owners were required to elect a distribution method on or before the required beginning date.** Taxpayers are no longer required to elect a method for receiving minimum distributions. The required distribution will automatically be the lowest possible amount.

- **Prior to the changes, IRA owners had to name a beneficiary on or before the required beginning date in order to take distributions over joint life expectancies.** Now, for purposes of calculating minimum required distributions, most taxpayers will use a uniform life-expectancy table (which uses a joint life assumption). These calculations will apply to all IRA owners, except those who are more than 10 years older than his or her spouse. In those cases, the IRA owner can use his or her (and his or her spouse's) joint life expectancy, allowing even lower minimum distributions.

- **It is no longer required that an IRA owner name a designated beneficiary on the date he or she starts taking withdrawals.** The IRA owner can also change his or her beneficiary at any time without affecting the amount of his or her minimum required distribution.

- **Lump sum distributions are no longer required when no beneficiary is named.** For example, if the IRA owner dies before he or she reaches age 70½ and he or she has not named a designated beneficiary, the IRS will allow the IRA owner's heirs up to five



years to withdraw the proceeds and pay taxes. Previously, the IRA proceeds had to be withdrawn by December 31st of the year after the IRA owner died, creating a severe tax burden to the heirs.

- **The mandatory date for distribution remains the same as before** (the IRA owner must withdraw the minimum required distributions by December 31st of each year). In addition, it's still critical that the IRA owner name a designated beneficiary; however, the IRA owner doesn't have to do it at any particular time, and the age of the beneficiary won't affect the amount of required distributions. After the IRA owner's death, the beneficiary must be established by December 31 of the following year. **BC**

The preceding article is only a brief summary of the revisions to the rules involving the timing of receipt of minimum distributions and for the determination of the amounts of those distributions. Properly identifying beneficiaries and secondary beneficiaries of IRAs, 401(k) plans and other retirement plans is an important part of the estate planning process. Please contact your Broad and Cassel estate planning attorney for more information on these subjects.



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