

# Estate Planning Alert

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Gerald Carp, center, with Tom Draper (left) and Jeff Goldman (right), comprise the Estates and Trusts legal team at Mazur, Carp & Rubin.

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## 2006 Estate Tax Changes

Federal transfer tax rates, exemptions and exclusions changed on January 1, 2006 as follows:

- The lifetime exemption from federal estate tax is now \$2 million per donor. This reflects an increase from the 2005 exempt amount of \$1.5 million per donor.
- The lifetime federal gift tax exemption remains at \$1 million per donor.
- The lifetime exemption from federal generation-skipping transfer tax increased to \$2 million per donor.
- The annual federal gift tax exclusion increased from \$11,000 to \$12,000 per donee. Now, each donor can give \$12,000 per year to any number of donees, free from federal gift tax implications. Properly coordinated, substantial estate tax savings can be achieved through the use of the annual exclusions.

Call us today to discuss how these exemptions can be made to work for you.

## NY Times' Story on Estate Tax Contained Errors

As we went to press, a story appeared in the Business section of *The New York Times* ("A Boon for the Richest in an Estate Tax Appeal," June 7, Page C8) regarding estate taxes that contained two major errors. Since many of our clients read the newspaper, we thought we'd use this space to give you the correct information. First, the article stated that under current law, the estate tax applies to persons who die with a net worth of more than \$1.5 million. In fact, the threshold for the imposition of the estate tax is \$2 million, not \$1.5 million. The \$1.5 million figure applied to estates prior to 2006 but the law changed to the \$2 million figure for 2006.

## Don't Fly Without Designating Beneficiary

Have you flown lately? A recent case from a New York Surrogate's Court highlights a frequent but little understood trap that many people can fall into when buying airline tickets: life insurance proceeds that are needlessly subjected to estate administration expenses and creditors' claims when the beneficiary designation is not properly completed.

Many of us own life insurance policies in which we expressly designate a beneficiary to receive the proceeds in the event of our death. However, many people purchase life insurance "on the fly", like travel insurance.

American Express, for example, provides \$1 million or \$2 million of life insurance for your air travel at a small cost added to your monthly bill. But people enrolled in these programs often fail to designate a beneficiary in the event of accidental death.



In the recent New York case, the decedent did not designate a beneficiary in his travel insurance policy, which triggered the policy default provision for payment of the insurance proceeds. (Most default provisions designate as beneficiary, in order, one's spouse, children, parents, siblings and if none, to the estate of the insured). The decedent's mother sought a ruling from a New York Surrogate's Court to prevent the father of their late child from receiving any life insurance proceeds because he had abandoned the decedent during infancy by not paying child support.

This case points to the need for diligence in designating beneficiaries of life insurance policies, lest it result in unnecessary and expensive litigation among family members. In addition, if the proceeds are paid to one's estate instead of a named beneficiary, the proceeds will be subjected to the estate's administration expenses, including executor's commissions and to the claims of creditors of the insured.

Let us inspect your life insurance policies and other testamentary instruments to assure that they provide what you want, and that they are coordinated with your overall estate plan, so that your hard earned property is not subjected needlessly to claims of creditors and estate taxes. Please call us for more details.

Second, the article said that "No estate tax is owed when the first spouse dies." Federal law states that if someone leaves property worth more than \$2 million, the estate is taxed unless the excess is expressly bequeathed to the surviving spouse by a will or other legal process. Money and/or property in excess of \$2 million bequeathed or passing to children, other relatives, and friends is fully taxable even if the spouse survives.

## Mazur, Carp & Rubin T&E Attorneys

**Gerald I. Carp, the chair of the Trusts and Estates Practice, is widely recognized for nearly four decades of experience in complex estate-related litigation for individuals and businesses, wealth protection/preservation and estate and trust administration. He has lectured and published widely on these topics.**

**Mr. Carp, a founding partner of the firm, is regularly called upon to litigate the validity of Wills, the rights of survivors to jointly held assets and insurance proceeds, as well as disputes among executors, trustees and beneficiaries. He also helps clients resolve disputes involving accountings of executors and trustees and closely held businesses.**

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**Thomas G. Draper, Jr. is a partner at the firm where he specializes in estate planning, probate and estate administration, and taxation. He is a member and former co-chair of the Section on Estates, Trusts and Surrogate's Court Practice of the New York County Lawyers' Association and currently chairs the Legislation and Government Regulation Committee of that section. He is also a member of the Trusts and Estates Section of the New York State Bar Association.**

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**Jeffrey A. Goldman, an associate at the firm, focuses on trust and estate litigation, estate and tax planning, and estate administration.**

**Mr. Goldman has handled matters involving complex wills and trusts, will contests, estate tax and fiduciary income tax planning and analysis, gift tax and generation-skipping tax planning and audits, trust accountings, establishing kinship and heirship, intestate estates, and matters involving estates of resident aliens and foreign nationals in the United States.**

**He also has particular experience with charitable 501(c)(3) entities and commercial litigation and has lectured on IRC Section 529 College Tuition Savings Plans.**

## 529Tuition Plans Can Help Reduce Taxes

Section 529 qualified tuition plans ("529 plans") allow a donor to either prepay tuition or establish an account to provide for a beneficiary's qualified educational expenses. There are two types of 529 plans: (i) prepaid tuition plans, and (ii) college savings plans. Though New York residents may enroll in 529 plans established by other states, there are certain income tax benefits available to New York taxpayers who contribute to accounts in New York's own 529 plan.

New York's 529 plan is known as a *529 savings plan*. A donor establishes an account on behalf of a beneficiary and then contributes money to the plan. The donor can choose from a variety of investments depending on the risk tolerance of the donor and the time horizon when the beneficiary will need to access the available funds.

The beneficiary can withdraw the funds when the beneficiary is ready to attend college (or another qualifying educational institution). So long as the funds are used for "qualified educational expenses" – generally: tuition, books, and certain room and board expenses – the withdrawn funds do not constitute income to the beneficiary. Thus, not only are the earnings and growth of the contributions to the account not subject to income tax while they are in the account, unlike a 401k retirement savings plan, the withdrawals are not taxable income to the beneficiary upon withdrawal!



### Tax Benefits to the Donor

There are two potential tax benefits to a New York taxpayer who contributes to New York's 529 plan in a given taxable year: (i) a New York income tax deduction of up to \$5,000 (or \$10,000 in the case of a married couple) per year, and (ii) a reduction to the donor's taxable estate. A New York taxpayer is entitled to dollar-for-dollar income tax deduction (up to a \$5,000 per year) against New York income tax for funds contributed to New York's 529 plan in a taxable year. No such deduction is available to a New York taxpayer for funds contributed to the 529 plans of other states and no deduction is available to the donor for federal income tax purposes.

Donors interested in reducing the amount of their gross estate for estate tax purposes may also want to consider establishing 529 savings plans for certain beneficiaries. Using the annual gift tax exclusion, donors may contribute up to \$12,000 per year, per beneficiary, to a 529 plan free of gift tax consequences. For example, someone with five grandchildren could create a 529 plan for each of them, and, using gift-splitting with his or her spouse, could contribute \$24,000 per year (\$12,000 by each spouse) per beneficiary. By doing so for five years, the donor could reduce his or her gross estate by \$600,000.

Unlike an outright gift to a minor or young person, however, funds contributed to a 529 plan are for a particular purpose: "qualified education expenses." Though funds in the account may also be withdrawn for "unqualified" purposes, such withdrawals are taxable income to the recipient, plus an additional 10% penalty. While this article explains some of the broad, general advantages of establishing 529 plans, there may be additional income, estate, gift or generation-skipping tax implications depending upon your situation. Please contact us for advice about integrating 529 plans into your estate plan.