CPA Client Tax Letter

Tax Saving and Planning Strategies *from your* Trusted Business Advisor[sm]

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Citation and Resource Guide

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New In-Plan Conversions

- The IRS answers FAQs on Roth 401(k)s, known as Designated Roth Accounts, at **www.irs.gov/Retirement-Plans/Retirement-Plans-FAQs-on-Designated-Roth-Accounts**.

Tax-Free Gains From Home Sales

- The fine points of the tax treatment on the sale of a principal residence are explained in IRS Publication 523, Selling Your Home, at **www.irs.gov/pub/irs-pdf/p523.pdf**.

Diversify 529 Accounts

- For The IRS explains the tax benefits of qualified tuition programs, known as 529 plans, in Publication 970, "Tax Benefits For Education," p. 33, at **www.irs.gov/pub/irs-pdf/p970.pdf.**

Maximizing Medical Deductions

- For the rules on medical deductions, see IRS Publication 501,"Medical and Dental Expenses," at **www.irs.gov/pub/irs-pdf/p502.pdf**.

Using the Work Opportunity Tax Credit

- The U.S. Department of Labor spells out the rules for claiming the WOTC at **www.doleta.gov/business/incentives/opptax/wotcEmployers.cfm**.

Practice Development Tip

Time to Review Life Insurance Trusts

From 1987 to 1997, the federal estate tax exemption was $600,000. Bequests to non-spouse heirs in excess of that amount faced taxes up to 55%.

The estate tax exemption has gradually increased since then while rates have fallen. Still, as recently as 2003 the exemption was $1 million, with rates as high as 49%.

Under the tax law passed in early 2013, that exemption was permanently set at $5 million, indexed to inflation in future years (it is $5.25 million in 2013), and the tax rate on excess assets is 40%. Therefore, relatively few clients have reason to be concerned about a sizable exposure to federal estate tax.

However, many clients still have irrevocable life insurance trusts (ILITs) that were created 10 or 20 years ago. Considering the current shape of federal estate tax law, this is an ideal time to contact clients to see if they have such trusts that should be updated.

Often, ILITs are designed to provide liquidity. A client who expected a $1 million estate tax obligation, for example, might have purchased a $1 million life insurance policy.

Held in trust, the policy's death benefits could escape estate tax as well as income tax. Then the trustee could lend $1 million to the estate or buy $1 million of assets from the estate, providing cash for the tax bill.

Such ILITs may no longer be needed for estate tax liquidity. If you discover you have clients with ILITs, you can explain the situation and see how the clients want to proceed.

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Clients may prefer not to keep paying life insurance premiums and trustee fees if estate liquidity is no longer necessary. If so, you might suggest clients meet with a knowledgeable attorney to see if the trust can be unwound, under state law.

On the other hand, keeping the ILIT in place can ensure that the client's heirs will receive a substantial inheritance at the client's death, tax-free. Clients who are concerned about leaving a legacy after possibly spending huge amounts on health care for many years may decide to leave the ILIT alone, providing peace of mind as they spend down assets.

Such client discussions need not be limited to ILITs. You also can ask about existing bypass trusts, qualified personal residence trusts (QPRTs), and so on. Clients may be grateful if you help them evaluate whether or not their old estate planning trusts should be retained or revised.

Questions or comments about the *CPA Client Tax Letter*? Need help with your subscription?

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