McNees Wallace & Nurick LLC

SEPTEMBER 2011

Harrisburg, PA • Lancaster, PA • State College, PA • Columbus, OH • Washington, DC

McNEES INSIGHTS
Asset Planning and Federal Taxation

BUDGET CONTROL ACT OF 2011

by Vance E. Antonacci

After much debate and brinkmanship, on August 2, 2011 President Obama signed the "Budget Control Act of 2011". The Act increases the federal government's debt limit by $900 billion and provides for $917 billion of spending cuts, which is achieved through the reduction of discretionary government spending over a ten year period (fiscal years 2012-2021, with the government's fiscal year 2012 beginning on October 1, 2011).

In addition, the Act establishes a Joint Select Committee on Deficit Reduction, which will consist of twelve members of Congress (six members of the Democratic party and six members of the Republican party). The purpose of the Joint Committee is to propose legislation by November 23, 2011 that will reduce the federal budget deficit by $1.5 trillion over fiscal years 2012-2021. If a proposal is made, the House and the Senate must each vote on the proposal "as-is" by December 23, 2011. If the Joint Committee's proposal is enacted, then the President would be authorized to request a debt limit increase of $1.5 trillion. If, however, the Joint Committee fails to produce a proposal or if its proposal is not enacted, then an additional $1.2 trillion of spending cuts will automatically occur and the debt limit increase is limited to $1.2 trillion. The automatic spending cuts apply to both mandatory and discretionary spending, but certain spending is exempt, such as social security, military and government employee retirement benefits, Medicaid and other welfare programs, and interest payments on debt.

A reduction in some government spending is inevitable based on the structure of the Joint Committee and the make-up of its membership. The unknown variable is whether the federal tax laws will change. The Republican members of the Joint Committee have vowed not to raise taxes while the President opposes any proposal that does not include tax increases. Possible changes to the tax laws include:

- Elimination of accelerated depreciation and bonus depreciation for businesses;
- Elimination of the LIFO method of accounting for inventory;
- Elimination of tax credits for certain industries or activities, such as oil and gas production and alternative energy;
- A reduction or elimination of deductions for individuals, such as the deduction for mortgage interest; and
- Changes in individual income tax brackets (most likely lower rates and less brackets in exchange for the reduction or elimination of deductions).

A few noteworthy issues with the Act and the Joint Committee:

- The automatic spending cuts will not occur until fiscal year 2013, which begins shortly before the next election cycle, so the impact of the cuts should not impede the re-election of the members of Congress.
- Comprehensive reform to the federal tax laws is an unlikely result of the Committee given the deadline for the Committee's proposal.
- Although the Committee proposal may include tax increases, any proposal may be rejected by either the House or the Senate or vetoed by the President.
- Whether the House or the Senate will reject tax increases is hard to gauge because the automatic spending cuts affect both Republican and Democratic priorities.
- The current Congress cannot bind any future Congress, so the proposal of the Joint Committee, if enacted into law, may only enjoy a short existence.
- If the Joint Committee fails to act or if Congress fails to adopt its proposal, then the President likely will let the "Bush" tax cuts enacted in 2001 expire (recall that these tax cuts were set to expire in 2010, but were extended until December 31, 2012).
- If the "Bush" tax cuts are allowed to expire as part of a Joint Committee proposal, any increase in revenue that results does not count against the $1.5 trillion of deficit reduction that is the mandate of the Joint Committee (current laws are not factored into the equation).
- There are several favorable tax laws, such as the AMT patch, that are set to expire this year and must be addressed (either as part of a Joint Committee proposal or otherwise). ■

Vance E. Antonacci practices in the McNees Asset Planning and Federal Taxation, Business Counseling, and Public Finance groups.
717.581.3701 / vantonacci@mwn.com

PLANNING AND PAYING FOR LONG-TERM CARE (PART 2 IN A SERIES: MEDICARE)

by Scott Alan Mitchell

As discussed in Part 1 of this series, the U.S. Department of Health and Human Services estimates that at least 70% of people over age 65 will need long-term care services at some point in their lives – and over 40% will need care in a nursing home for some period of time. In Pennsylvania, the cost for nursing care is nearly $8,000 per month. Nursing care generally is paid either out of one's private assets, Medicare and private health insurance, long-term care insurance, or Medicaid/ Medical Assistance. Medicare and private health insurance will be the focus of this Part 2. According to current statistics, approximately 20% of nursing care throughout the country is paid by Medicare. However, as will be explained below, that statistic is somewhat misleading in that Medicare coverage for nursing care is quite limited.

Many individuals mistakenly use the terms "Medicare" and "Medicaid" interchangeably, but they are entirely different programs. Medicare is a health insurance program generally for people age 65 and above. People under 65 with certain types of disabilities also can qualify for Medicare. Medicare generally has four "parts," but the most common parts are Part A (hospital insurance) and Part B (medical insurance). For most individuals 65 or older, if they receive or are eligible to receive Social Security benefits, they are entitled to Medicare Part A completely free of charge (and others may be able to "buy-in" to Part A). Anyone who is eligible for free Part A also may enroll in Medicare Part B by paying a monthly premium (currently $96.40 or $110.50 for most individuals).

Medicare Part A (hospital insurance) provides coverage for inpatient care in hospitals, skilled nursing facilities, hospice, and home health care. With respect to skilled nursing facilities, Medicare Part A only pays for skilled nursing care if the need for nursing care arises after an inpatient stay in a hospital for at least three days ("observation" status or time spent in the ER does not count; inpatient status is required). Thereafter, so long as the person is receiving rehabilitation in the nursing facility, Medicare Part A will pay for a maximum of 100 days of skilled nursing care. The first 20 days will be covered in full by Medicare. Days 21 through 100 will be covered partially by Medicare, subject to a daily co-payment (presently $141.50). The co-payment generally is paid by the individual's private/secondary health insurance. However, individuals without secondary health insurance must pay the daily co-payment out-of-pocket (over $4,000 per month).

As mentioned above, Medicare coverage will cover only up to 100 days – and that coverage only occurs so long as the person is receiving rehabilitation for the illness for which he or she was hospitalized. Thus, if an individual refuses therapy while in the nursing facility, Medicare will end coverage before the full 100 days. Also, if an individual's rehabilitation or improvement has ceased or reached a plateau while in the nursing facility, Medicare will end coverage before the full 100 days. When Medicare coverage ends, the individual's private health coverage usually also ends. Although many individuals mistakenly believe that the first 100 days of nursing care automatically are covered by Medicare, current statistics suggest that Medicare coverage typically ends after 25 to 30 days. When Medicare coverage is about to end, an advance "notice of non-coverage" generally will be provided, which the individual may appeal if he or she believes that Medicare coverage should continue.

Medicare will cover subsequent nursing facility stays so long as the individual is admitted to the nursing facility following a new 3-day inpatient hospital stay – and so long as the person previously has been out of a hospital or nursing facility for 60 days.

As can be seen above, Medicare certainly is beneficial for those needing a short-term nursing care stay after hospitalization. However, for those needing long-term care in a nursing facility, Medicare coverage is very limited – lasting only as long as the person is receiving rehabilitation, and up to a maximum of only 100 days. Thus, the individual generally will be left with payment options of private pay, long-term care insurance, and Medicaid/Medical Assistance. In Part 3, long-term care insurance will be discussed. ■

Scott Alan Mitchell practices in the McNees Asset Planning and Federal Taxation, and Business Counseling groups.
717.581.3713 / smitchell@mwn.com

ESTATE PLANNING – PORTABILITY PROVISIONS OF TRA 2010

by Frank C. Chesters

The "Tax Relief, Unemployment Insurance Authorization, and Job Creation Act of 2010" was enacted December 17, 2010 and is referred to as "TRA 2010." For calendar years 2011 and 2012, TRA 2010 reunified the estate, gift and generation-skipping taxes with a $5 million exemption and a 35% tax rate. The $5 million exemption will be indexed for inflation in calendar year 2012 only. If Congress fails to enact additional legislation by December 31, 2012, the taxes will remain unified but will be reduced to an inflation-adjusted $1 million exemption and increased to a 55% maximum tax rate.

Until TRA 2010 was enacted, married couples typically implemented a two-trust estate plan to take advantage of each spouse's estate tax exemption. When the first spouse passed away, a credit-shelter trust would be funded first with an amount up to the deceased spouse's estate tax exemption. A marital trust qualifying for the marital deduction would be funded if the value of the deceased spouse's assets exceeded the estate tax exemption thereby deferring the payment of any estate tax. When the surviving spouse subsequently died, the combined value of the assets in the deceased spouse's marital trust and the surviving spouse's assets would be subject to the estate tax only to the extent it exceeded the surviving spouse's estate tax exemption. The assets in the credit-shelter trust would not be subject to estate tax when the surviving spouse died, no matter how much the assets grew in value. Most importantly, in the event the estate tax exemption of the spouse who died first was not fully utilized when he died, i.e. the credit-shelter trust was not fully funded with assets having a value equal to the estate tax exemption, the unused amount of the deceased spouse's estate tax exemption was lost. The worst outcome for clients who failed to implement an estate plan designed to reduce their exposure to the estate tax was that the estate tax exemption of the spouse who died first was totally lost, and the surviving spouse only had her remaining estate tax exemption to use when she died.

TRA 2010 made a significant change to the estate tax by adding the concept of "portability." The executor of the deceased spouse's estate may transfer any unused amount of the deceased spouse's estate tax exemption to the surviving spouse. The executor of the deceased spouse's estate must file an estate tax return (Form 706) on a timely basis, that is on or before nine months following the date of death, and make an election to permit the surviving spouse to utilize the unused estate tax exemption. When the surviving spouse subsequently dies, her estate tax exemption is increased by the "deceased spousal unused exclusion amount," referred to as "DESUEA." Therefore, if the first spouse of a married couple dies during calendar years 2011 and 2012, especially for married couples who do not have the two-trust estate plan discussed above, consideration must be given to preparing and filing a Form 706 to make this election. Failure to do so on a timely basis will prevent the surviving spouse from having the DESUEA available at her death.
What if the first spouse of a married couple dies during calendar years 2011 and 2012 and a two-trust estate plan is in place? Many of these types of estate plans have been structured in recent years to allow the surviving spouse the flexibility to determine whether to fund the credit-shelter trust by the use of one or more disclaimers within the nine-month period following the deceased spouse's date of death. The following benefits may be realized by the surviving spouse by choosing to fund the credit-shelter trust:

- Post death appreciation of the assets in the credit-shelter trust will be sheltered from the estate tax.
- Trust assets will be protected from creditors.
- Trust assets may be protected when the surviving spouse remarries, assuming the surviving spouse is not the sole trustee of the credit-shelter trust.
- Portability ends after December 31, 2012, unless extended by future legislation.

Portability applies for the gift tax exemption as well as the estate tax exemption. Therefore, use of the deceased spouse's DESUEA would have significant benefits to the making of lifetime gifts by the surviving spouse. However, portability does not apply to the generation skipping tax exemption. Therefore, for clients who want an estate plan that takes advantage of the planning opportunities of generation skipping, the funding of the credit-shelter trust of the spouse who dies first would be important.

In the "General Explanations of the Administration's Fiscal Year 2012 Revenue Proposals" (February 14, 2011), the Treasury Department explained how the President's 2012 budget proposals presume several important changes in the estate, gift and generation-skipping taxes. These changes included making "portability" of the deceased spouse's DESUEA permanent. However, we have no ability to predict whether Congress will enact such legislation. Therefore, it is important for clients to continue to be proactive in addressing their estate plans. Clients should not rely on the portability provision for solving their estate tax exposure in coming years. ■

Frank C. Chesters practices in the McNees Asset Planning and Federal Taxation group.
717.581.3702 / fchesters@mwn.com

McNEES WELCOMES KENDRA McGUIRE

The Asset Planning and Federal Taxation group welcomes Kendra McGuire to McNees. With over 20 years experience as a litigator, Kendra focuses her practice in Orphans' Court litigation matters for clients that include financial institutions, shareholders, educational organizations, healthcare institutions, charities and individuals. Kendra works with trust officers, estate administrators, financial institutions, financial advisors, brokers, colleges and educational institutions, charities, investment advisors, financial planners, securities firms, and individuals to assist them in all matters related to their role as a fiduciary, stakeholder or beneficiary. She litigates in Orphans' Courts throughout Central and Eastern Pennsylvania. Serving as counselor, advisor and litigator, examples of Kendra's work for clients include surcharge actions, fee and commission disputes, trust reformations, risk and liability avoidance counseling, *cy pres*, foundation work, will contests and guardianships.

SUBSCRIBE FOR EMAIL DELIVERY

To receive the *McNEES INSIGHTS* Newsletter in your email please go to the "newsletter signup" page under the "newsroom" tab at www.mwn.com.

McNees Asset Planning & Federal Taxation Group

David M. Watts, Jr., Chair 717.237.5344/dwatts@mwn.com	Bradley J. Gunnison 717.237.5479/bgunnison@mwn.com	Scott Alan Mitchell 717.581.3713/smitchell@mwn.com	Richard W. Stevenson 717.237.5208/rstevenson@mwn.com
Vance E. Antonacci 717.581.3701/vantonacci@mwn.com	Veronica R. Johnson 717.237.5417/vjohnson@mwn.com	Elizabeth P. Mullaugh 717.237.5243/emullaugh@mwn.com	M. Yvonne Crouse, Paralegal 717.581.3732/ycrouse@mwn.com
Salvatore J. Bauccio 717.237.5238/sbauccio@mwn.com	Donald B. Kaufman 717.237.5373/dkaufman@mwn.com	James K. Noel, IV 717.581.3709/jnoel@mwn.com	Linda M. Eshelman, Paralegal 717.237.5210/leshelman@mwn.com
Frank C. Chesters 717.581.3702/fchesters@mwn.com	Peter F. Kriete 717.237.5486/fkriete@mwn.com	J. Corey Reeder 814.867.8500/creeder@mwn.com	David E. Gruver, Paralegal 717.237.5362/dgruver@mwn.com
Timothy M. Finnerty 717.237.5394/tfinnerty@mwn.com	Kendra D. McGuire 717.581.3734/kmcguire@mwn.com	Bruce R. Spicer 717.237.5331/bspicer@mwn.com	Dianna L. McSherry, Paralegal 717.581.3707/dmcsherry@mwn.com

© 2011 McNees Wallace & Nurick LLC
McNEES INSIGHTS is presented with the understanding that the publisher does not render specific legal, accounting or other professional service to the reader. Due to the rapidly changing nature of the law, information contained in this publication may become outdated. Anyone using this material must always research original sources of authority and update this information to ensure accuracy and applicability to specific legal matters. In no event will the authors, the reviewers or the publisher be liable for any damage, whether direct, indirect or consequential, claimed to result from the use of this material.