OBJECTIVES OF ESTATE PLANNING

While Living:

Provide instructions in advance in case of disability or lingering illness.
- Avoid a living probate - conservatorship
- What life sustaining measures do you desire, etc.

At Death:

Name a guardian for minor or dependent children.
Give instructions for the distribution of assets.
Avoid time delays and unnecessary red tape.
Avoid Publicity.
Provide peace of mind.
Reduce or eliminate probate costs.
Avoid or reduce taxes:
- Estate taxes,
- Income taxes,
- Generation-skipping transfer taxes, and
- Retirement plan penalties for excess accumulations

<u>Your Estate Consists Of:</u> (Probate and Estate Tax Estates Can Differ Greatly)

All Tangible Assets

House
Real Estate
Auto
Jewelry
Personal Possessions

All Intangible Assets

Bank accounts
Annuities
Stocks, Bonds
Mutual Funds
Partnership interests
Retirement plan proceeds
<u>Life Insurance face amount</u>

DISTRIBUTION OF ASSETS

After our death, how do our assets get to the people we wish to receive them?

1. **OPERATION OF LAW**
2. **PROBATE (With or without a will)**
3. **TRUST (s)**

Operation of Law

The law directs certain assets to pass directly to your survivors, outside of the probate process. These assets are not controlled by the will. They are not part of probate. They go directly to the designated survivor.

Examples

1. Property held by you and your spouse (or others) as joint tenants with the right of survivorship, etc.
2. Where a beneficiary has been designated.
   - A. Life Insurance
   - B. Retirement Plans, including IRAs, 401(k)s, TSAs
   - C. Annuities
   - D. Totten Trust Accounts (ITF Accounts - in-trust-for)
   - E. P.O.D. Accounts (payable-on-death)

If your estate is the beneficiary, the proceeds will be probated.

PROBATE

The court process of distributing your property to your survivors and creditors after your death.

When there is no will, state guidelines determine how probate assets are distributed. This may or may not be how you would like.

If you have a will, probate's function is to carry out the instructions in your will.

Advantages of Probate

1. Distributes probate estate assets as you wanted (assuming valid will exists).
2. Usually, time for challenging the will is limited.
3. Usually, time for creditors to make claims on the estate is limited.
4. Court supervises the executor's actions.

Disadvantages of Probate

1. Survivors cannot access most probate assets during probate period, which can be a year or more.
2. Court fees, attorneys fees, executor fees, accounting fees and appraisals may cost from 3% to 7% of the value of the estate.
3. Probate files are open to the public in most states.

Property Passing Through Joint Tenancy Only Receives Tax Basis Step-up to Fair Market Value on Decedent's Share of Asset. Taxable Gain in survivor's share remains.

Community Property receives tax basis step-up to fair market value on both decedent's half and surviving spouse's one half. That allows surviving spouse to sell such property immediately after decedent's death for little or no capital gain.

WHAT IS A TRUST?

A trust is formed when one party (**settlor, grantor, trustor**)
transfers property to a second party (**trustee**)
who must use the property solely for the benefit of a third party (**beneficiary**).

The same person(s) can be the settlor, trustee and beneficiary of the trust.

<u>There are several types of trusts,</u> both <u>inter vivos (living)</u>, and <u>testamentary (at death).</u>

The most common reason for including a testamentary trust in a will is to provide for dependent children. You can specify who will manage the trust funds, for what purposes the funds may be used, and when they will be paid out.

The revocable living trust can be used to transfer property outside of probate and the will.

REVOCABLE LIVING TRUST

<u>Advantages</u> of a Revocable Living Trust

1. Avoids the costs and time delays of probate (including separate probates in each state where real property is located).
2. Activities are not on public display at the courthouse, unlike a probate.
3. A trust (living or testamentary) allows much more detailed instructions to be given regarding the use and distribution of assets, than is possible under a will. With a will, minor children generally receive inheritance at age 18. With a trust, you can provide distributions for special purposes, subject to conditions, and spread out over time, or distributed immediately upon death.
4. A living trust can provide for the management of your estate while you are living, if you can no longer take care of it yourself (avoids living probate).
5. A trust (living or testamentary) can help a married couple to save estate taxes.
6. Consolidation of Estate Plan. All assets pass according to central plan.

<u>Disadvantages</u> of a Revocable Living Trust

1. More time and expense to establish.
2. May not reduce estate tax liability if written improperly.
3. Fear of giving up personal ownership of one's assets (not a big problem).

Using A Bypass Trust

A Bypass Trust can be used to divide an estate between spouses in order to reduce or eliminate estate taxes at the death of the second spouse.

The Unlimited Marital Deduction provides an estate tax deduction for all property left to a (U.S. citizen) surviving spouse upon the first spouse's death. So there is usually no estate taxes due at the first death.

How and When are Estate Taxes Paid? Estate taxes are due and payable in cash within nine months after death.

How Much Are Estate Taxes? A credit shelters the first <u>$1,500,000</u> of the taxable estate. That is scheduled to gradually increase, and then revert to $1,000,000 in 2011. That amount can be reduced by taxable lifetime gifts. Present gifts of less than $11,000 per person, per year are not taxable.

Amount of Taxable Transfer	**Applicable Rate**
Less than $1,000,000	0%
$1,000,000 to $1,250,000	41%
$1,250,000 to $1,500,000	43%
$1,500,000 to $2,000,000	45%
$2,000,000 to $2,500,000	49%
$2,500,000 and over	50%

A Bypass Trust is used to take advantage of $1,500,000 credit at the first death and keep those assets out of the surviving spouse's estate, although they are still controlled by and used for the benefit of that spouse. Those assets are placed into the bypass trust for the surviving spouse's benefit and **bypass** the surviving spouse's estate taxes, regardless of how much they increase in value.

That allows the surviving spouse an additional $1,500,000 credit to shelter the remaining assets from estate taxes at the second death. That doubles the estate that can pass free of estate taxes to <u>$3,000,000.</u> That can save **$675,000**.

Irrevocable Insurance Trust (Similar to bypass trust)

<u>Big Surprise</u>: Face value of life insurance proceeds are part of taxable estate.

Loss of control not an issue because assets not meant for insured's use anyway.

A trust similar to the bypass trust is formed to own the insured's life insurance. If properly formed, it is not part of the insured's taxable estate. By using provisions similar to the bypass trust, it can also be kept out of the surviving spouse's estate, although it is available for that spouse's benefit. It can also benefit children or other heirs and provide liquid funds to pay the estate taxes on the other estate assets.

Payment of Premiums. The insured gifts enough money to the trust for it to pay the insurance premiums. By using "Crummey" provisions, these gifts can be gift tax exempt under the $11,000/year/person exemption, so they don't reduce the $1,500,000 lifetime credit.

Other Lifetime Giving

Making maximum use of the $11,000 annual exemption amount by giving liberally to heirs during lifetime.

Combining with Limited Partnership or LLC

If family assets are transferred to a limited partnership or LLC, Parents can give shares in the partnership each year, without losing control of the assets, since they are the controlling partners or members. The assets inside the partnership are protected from seizure from the heirs creditors. Discounting can be used to expand the size of the annual gifts.

Qualified Personal Residence Trust Gifting

Charitable Giving