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Estate Planning Concepts

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Keep Your Estate Plan Flexible

Estate planning has become more difficult in recent years due to changing estate tax laws. Estate tax rates and exemption amounts keep changing, increasing to $3,500,000 this year. Next year, the estate tax will be repealed, but it will be reinstated in the following year, based on 2001 tax laws. All these changes can make it difficult to determine whether your estate plan should be revised due to new changes. Thus, it is increasingly important to build flexibility into your estate plan. Some points to consider include:

❍ **Find ways to incorporate changing exemption amounts in your estate plan.** Many estate planning documents indicate that trusts should be funded with assets equal to the estate tax exemption amount or generation-skipping transfer tax exemption amount. Evaluate whether those amounts are still appropriate considering their current high levels. Those amounts may leave more than intended to certain heirs or may place so much in a credit shelter or other trust that your spouse may receive very little of your estate outright. You may want to set a cap on the amounts placed in trust, even if that means you won't fully utilize your exemption amounts.

❍ **Make sure you have enough solely owned assets to fund these trusts.** Once you have decided how much should be placed in trust, make sure you have sufficient assets titled in your own name. Assets that you own jointly with your spouse or another individual will automatically go to that person, rather than to the trust, after death.

❍ **Consider adding a disclaimer provision to your estate planning documents.** This provision details what will happen if one of your heirs disclaims his/her inheritance. That way, your heirs can decide after your death how much should be placed in various trusts. For instance, a husband can leave all his assets to his wife with the condition that any disclaimed

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What Are PODs and TODs?

After your death, you may want your heirs to gain access to money in bank and investment accounts without going through the probate process. One way to accomplish that is to make one of your heirs a joint owner on the account. However, while you are alive, that heir can legally withdraw part or all of the assets without your knowledge, or the assets could be put at risk if that heir encounters credit problems. Also, after death, the assets will go directly to the joint owner, who is not obligated to distribute the funds to other heirs. Even if that person wants to distribute the assets to other heirs, it will be considered a gift from that heir to the other heirs, which may result in unintended gift tax consequences.

A better solution may be to use payable-on-death (POD) accounts for bank accounts and transfer-on-death (TOD) registrations for investment accounts, which name beneficiaries for these accounts. While you are alive, the beneficiaries have no claim to the assets in these accounts. After your death, they gain immediate access to the accounts by showing identification and your death certificate.

With these designations, the assets will be distributed to the beneficiaries listed on the accounts, not by your will's provisions. Thus, you need to coordinate these designations with your overall estate plan, so that one or more heirs won't receive more in total assets than you intended. ❍❍❍

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Estate Plan

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assets go into a trust paying her income for life, then passing the principal to their children after her death. This gives the wife the opportunity to divide assets based on her needs and wishes at the time of her husband's death.

❍ **Review your gifting strategies.** You may still want to continue gifting strategies to utilize your annual gift tax exclusion ($13,000 in 2009 or $26,000 if the gift is split with your spouse) and your lifetime gift exclusion amount. For those with estates large enough to be subject to estate taxes, these strategies remove assets from your taxable estate without paying any gift taxes. When using your lifetime exemption amount of $1,000,000, look for ways to maximize your tax-free gift. For instance, individuals who transfer noncontrolling interests in businesses, farms, real estate, and other assets during their lifetime may be able to assign a minority interest discount to the gift's value. By gifting assets to certain types of trusts, such as qualified personal residence trusts and grantor retained annuity trusts, you can place an asset in trust now, retain use of the asset for a period of time, and assign a lower value to the gift.

❍ **Consider making charitable contributions during your lifetime.** While charitable contributions made after death are free of estate taxes, that may not be a consideration due to higher exemption amounts. Charitable contributions made during your lifetime will still lower your taxable estate, and you'll receive a current income tax deduction.

❍ **Reevaluate your life insurance needs.** Since the estate tax will only be repealed for the year 2010, you may still want life insurance to help your heirs pay estate taxes. Even if you die in the year 2010, any inherited assets will not receive a step-up in basis, perhaps leaving your heirs with a large capital gains tax burden.

❍ **Review how specific assets are distributed.** In 2010, inherited property will have a basis equal to the lesser of the decedent's adjusted basis or the property's fair market value at the decedent's date of death, with three exceptions: 1) $1,300,000 of basis can be added to assets. 2) Unused capital losses, net operating losses, and certain built-in losses can increase this cap. 3) An additional $3,000,000 of basis can be added to assets inherited by a surviving spouse. Due to these exceptions, you may want to specifically allocate assets with low bases to your spouse and assets with a higher bases to other heirs to ensure the step-up in basis is maximized.

❍ **Go over your entire estate plan at least every three years.** No matter how much flexibility is built into your estate plan, you should still thoroughly review your plan every three years or so. Even if there are no major changes in the estate tax law or your personal situation, such as a marriage, death, divorce, or birth, gradual changes in your situation, such as an increasing net worth or a decline in your investment portfolio, may make changes to your estate plan necessary.

Please call if you'd like to discuss strategies to increase flexibility in your estate plan. ❍❍❍

Be Prepared for a Layoff

In these economic times, job security is a notion from the past. All workers should be prepared financially for the possibility of a job layoff. Here are some tips to help with that process:

❍ **Stay on the lookout for signs of potential cutbacks.** Those signs could include layoffs at competitors, declining financial performance, top management changes, or a major tightening of expenditures. Under federal law, only companies with more than 100 workers are required to give 60 days notice of layoffs or plant closures.

❍ **Set up a cash reserve of at least three to six months of living expenses.** It typically takes at least that long to find a new job. It may take even longer in this economic environment or if you are middle-age or older.

❍ **Apply for a home-equity line of credit or other type of loan.** It is usually easier to obtain credit when you are employed, so get borrowing options in place to help during a layoff.

❍ **Look for ways to cut your living expenses.** Avoid nonessential expenses like extravagant vacations, clothing, and entertainment. Even if you aren't laid off, you can use those savings to increase your retirement savings.

❍ **Keep your resume up to date.** While you may not want to actively start looking for another job, be aware of the current job market and expand your professional contacts.

❍ **If faced with a layoff, don't just accept your employer's severance package.** Try to negotiate for more severance pay or for an extension of your health insurance benefits. Also check whether the company offers services to help you find another job.

Please call if you'd like to discuss this topic in more detail. ❍❍❍

Serving as an Executor

When you are asked to serve as executor of someone's estate, it is generally meant as a compliment that the person trusts you to serve in this important role. But don't simply accept without giving the matter serious thought. Not only does the job come with significant responsibilities, you may find yourself in the middle of family squabbles. Before agreeing to take on this role, consider the following:

Understand the duties involved. Those duties include:

- ❍ **Locating and valuing all assets.** This includes dealing with the probate court and filing all required documents; preparing a complete inventory of assets; notifying life insurance companies of the death; collecting money owed from employers, pensions, Social Security, and other sources; and arranging for property appraisals. While the will is in probate, the executor is responsible for maintaining and investing the assets. If a family business is involved, the executor may need to manage or liquidate the business.
- ❍ **Paying the estate's obligations.** This includes paying creditors; arranging for the family's immediate living expenses; and preparing and filing all income, estate, and inheritance tax returns. If assets must be sold to pay debts, the executor must decide which assets and when to sell them.
- ❍ **Distributing the estate.** The executor must decide when and how to distribute the estate's assets to the heirs. The executor may have to resolve conflicts among family members. After the assets are distributed, a final accounting must be prepared for the court.

Look for possible problems. In most situations, executors perform their duties with no issues. However, think carefully before accepting in the following situations:

- ❍ **The person is unwilling to show you his/her estate documents.** Without knowing all the details about the estate, you can't determine whether heirs may disagree or whether the estate is more complex than you are comfortable handling.
- ❍ **An heir is disinherited or heirs receive substantially unequal distributions.** While it is certainly within the person's rights to disinherit an heir or make unequal distributions, those situations are more likely to lead to court battles. Decide whether you want to get involved in that type of situation.
- ❍ **The person isn't well organized.** One of your primary duties is to track down, manage, and distribute assets. If the individual doesn't have his/her affairs well organized, you could spend excessive time hunting for documents and assets. ❍❍❍

Something for Everyone

I'd like to ask all of my clients to do a good deed. After reading this newsletter, please pass it along to a friend, coworker, or family member who could also benefit from it. Whether it is about keeping your estate plan flexible, parents or grandparents who need to do estate planning, or young parents who need to plan for their children, this newsletter has something for everyone, at any age.

Future newsletters will cover a wide variety of topics helpful for people of any age and estate planning situation. You could give it to anyone. Maybe just reading an issue will motivate them to make positive changes and begin planning for the future. So, do someone a favor, and pass this newsletter on.

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Using Lifetime Gifts

Lifetime gifts have long been used to reduce taxable estates, thus reducing estate taxes. But with the uncertainty surrounding the estate tax, are lifetime gifts still a viable estate planning strategy? Since it is scheduled to be repealed for one year only and then reinstated in 2011, you may still want to make gifts during your lifetime to reduce your taxable estate. Some tips to consider include:

- **Use your annual gift tax exclusion.** Every year, you can gift a specific amount ($13,000 in 2009, $26,000 if the gift is split with your spouse) to any number of individuals free of gift taxes. This amount is adjusted for inflation annually, in $1,000 increments. Over a number of years, an annual gifting program can remove substantial assets from your estate. For instance, if you and your spouse have three married children with two children each, you can gift $312,000 annually ($26,000 for each child, child's spouse, and grandchild). Any future appreciation or income generated on those gifts is also removed from your estate.

- **Pay medical and educational expenses.** Amounts paid directly to institutions for these expenses can be made gift-tax free, in addition to your annual gift-tax exclusion amount.
- **Consider using your lifetime gift exclusion.** This exclusion is $1,000,000 and is in addition to your annual gift-tax exclusion. Thus, those with estates large enough to be subject to estate taxes should consider using this exclusion to remove assets from their taxable estate. This also removes any future appreciation or income generated on those gifts from your estate. Lifetime gifts over $1,000,000 are subject to gift taxes, with the maximum gift-tax rate equal to the maximum estate tax rate in 2009 and then equal to the maximum individual income tax rate.
- **Consider delaying taxable gifts.** With the estate tax exclusion amount set at $3,500,000 in 2009 and the estate tax repealed in 2010, more estates will be able to avoid the payment of estate taxes.
- **Gift property that has the potential to increase in value but has not already done so.** A lifetime gift's tax basis remains your original basis plus any gift tax paid. Thus, if you gift an asset with a low basis, your heirs could owe significant capital gains tax when the asset is sold. However, keep in mind that through 2010, taxpayers in the 10% or 15% tax bracket pay 0% capital gains tax. If you have an asset that you intend to sell in the short term for the benefit of heirs who are in a low tax bracket, it may make sense to gift the asset to them, so they can sell it and pay no capital gains tax.
- **Make charitable contributions during your lifetime.** Charitable contributions made after death are free of estate taxes, making them a significant component of many estate plans. But if you make those contributions during your lifetime, you still reduce your taxable estate and receive an income tax deduction for the contributions.
- **Keep your own needs in mind.** While gifting can be a valuable estate planning strategy, you don't want to gift so much of your estate that you have difficulty making ends meet later in life. ❍❍❍

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