



The Top 10 Things You Need to Know About Estate Planning

Andrew M. Berger

3111 Stirling Road
Ft. Lauderdale, Florida 33312-6525
Tel: 954.364.6074
Fax: 954.985.4176
aberger@becker-poliakoff.com

Introduction

Over 200 years ago, Benjamin Franklin observed that “in this world nothing can be said to be certain, except death and taxes.” Never in his wildest dreams could Franklin have imagined “death and taxes” combining in a way quite like the estate tax does today. Although not much can be done about the certainty of death, many planning opportunities are available to reduce, if not avoid, the estate tax, while ensuring that your assets are transferred exactly as you wish. Even if the value of your assets is less than the amount you may pass free of estate tax (known as the applicable exclusion amount), which in 2009 is \$3,500,000, it is critical that you have certain basic planning documents. This article will explain how everyone can benefit from having an estate plan and highlight the top 10 things you need to know.

1. Taxes Aside, Don't Let the State Determine who Receives Your Assets and Custody Over Your Children!

If you die without an estate plan, the state's laws of intestacy will govern who receives your assets. Moreover, if you have minor children, the state will appoint a guardian to take custody of them and to manage any funds for their health, education, maintenance and support. Since there is no assurance that the distribution of your property will be directed in the manner you desire and that the custody of your children will be awarded to the people you would have selected, it is critical that everyone at the very least have a will. It should be noted that

planning is especially important to avoid unintended consequences in special situations, where, for instance, there has been a divorce or separation and the non-custodial spouse may have rights and intentions that conflict with yours.

2. If You are Married and Have a Combined Net Worth in Excess of the Applicable Exclusion Amount, Not Having a Credit Shelter Trust Could Cost You \$1,575,000 in Taxes.

Almost every married couple whose estate value exceeds the applicable exclusion amount benefits from the use of a credit shelter trust, also known as a by-pass or family trust. While a married couple could avoid estate tax completely at the death of the first spouse simply by transferring property to the surviving spouse and using the unlimited marital deduction to shield that transfer from tax, doing so would forfeit the use of the decedent spouse's applicable exclusion amount and increase the surviving spouse's taxable estate.

A credit shelter trust is used to ensure utilization of both spouses' applicable exclusion amounts, while still allocating the benefits of the trust property to the surviving spouse during his or her lifetime. Essentially, the first spouse to die leaves an amount equal to the applicable exclusion amount in trust for the benefit of the surviving spouse, who receives all of the trust income each year. Because the first decedent bequeaths assets to the credit shelter trust

rather than outright to the surviving spouse, the first spouse's applicable exclusion amount applies to the trust. For this reason, the funds in the trust (i.e., the principal of the trust) can pass tax-free to the couple's children upon the death of the surviving spouse without impacting the surviving spouse's remaining applicable exclusion amount. In other words, the funds in the credit shelter trust are never deemed transferred to the surviving spouse, so that such funds escape taxation in the surviving spouse's estate. Thus, the applicable exclusion amount to which each spouse is entitled gets utilized, effectively doubling the amount excluded from estate tax. In 2009, this amount is \$3,500,000, which equates to a savings of \$1,575,000 with the current estate tax rate of 45%.

3. Planning for Disability: You Should Have a Power of Attorney.

A power of attorney is a document that allows you to designate a representative, known as an "attorney in fact," to perform certain actions for you should you become ill, incapacitated or otherwise unable to manage your affairs. The representative could, for example, pay bills, sell securities or make major financial decisions on your behalf, depending on how broad or narrow you limit the powers. Without a power of attorney, your spouse or other loved ones would have to endure the delay and expense of seeking court approval to carry out needed financial transactions.

4. To Pull The Plug or Not to Pull the Plug, that is the Question You Want to Answer: The Need for a Living Will and Designation of Health Care Surrogate.

As the Terri Schiavo case illustrated, Florida law generally requires "clear and convincing evidence" of an incompetent person's medical preferences before life-sustaining treatment can be withheld or withdrawn. A living will and a designation of health care surrogate satisfy this clear and convincing

evidence standard and are critical to protect your right to self-determination. A living will is a written declaration of what life-sustaining medical treatment you will allow or not allow in the event you become incapacitated. For example, you may request that artificial nourishment be or not be withheld if you are terminally ill. Family members and medical institutions often challenge the validity of living wills, so it is critical both that they be properly drafted to include certain required language and also that they be executed with the proper formalities.

The designation of health care surrogate authorizes a person to make medical decisions on your behalf, and in many respects is a superior tool in carrying out a person's intent. While a living will provides instructions only with respect to life sustaining procedures, the person designated as the health care surrogate is authorized to make any health-care decision when the principal is unable to do so and may be authorized to request special treatment or care. It is often most effective to have both a living will and a designation of health care surrogate, which approach ensures that an advocate is present to carry out your wishes.

5. Life Insurance Demystified: If You Own a Life Insurance Policy in Your Own Name, the Government May Take 45 Percent of the Proceeds Upon Your Death.

Although it is generally known that life insurance proceeds are not subject to income tax, people are often surprised to learn that proceeds from life insurance policies are includable in the gross estate of the policy owner for estate tax purposes. To avoid this result, it is often advisable to create an irrevocable life insurance trust (ILIT) to own the life insurance policy. By utilizing an ILIT, the terms of which prevent the insured from changing the beneficiaries or exercising any other incidents of ownership in the policy, the proceeds of the policy will be effectively

removed from the insured's gross estate. This is true even though the insured gives the money to the trustee of the ILIT to pay the premiums of the insurance policy.

6. Probate is Avoidable: Consider Forming a Revocable Living Trust.

A revocable trust acts as a will substitute and is a written declaration and contract in which you state that you (as "grantor") are transferring your property into a trust for the benefit of yourself during your lifetime and then for the benefit of your heirs. The main advantage to a revocable living trust is the avoidance of probate, a costly, time consuming and public court proceeding in which your property is transferred to your heirs. Since only assets you own at the time of your death are required to be probated, and assets placed in a revocable trust are treated as owned by the trust, assets held by the trust are not subject to probate.

Another practical reason for having a revocable trust is to provide for the possibility of your becoming disabled. If all of your property is held in a revocable trust and you become disabled, the successor trustee that you named in the trust document can step in and manage your property for your benefit in accordance with the terms of your trust. This avoids, in most cases, the need to have a conservator appointed by the court to manage your affairs in the event of your incapacitation.

7. Title to Assets.

It is critical that clients periodically review the legal form in which they hold title to their business and personal assets in order to both minimize the exposure of such assets to the claims of potential creditors and to ensure that each spouse is able to effectively utilize his or her applicable exclusion amount. In addition, certain forms of joint ownership can be useful in avoiding probate and in disability planning.

8. Opportunities for Lifetime Gifting.

The Internal Revenue Code provides two basic mechanisms for transferring property free of gift tax: (1) the lifetime gift tax exemption, and (2) the annual exclusion amount. Every U.S. person has a \$1,000,000 lifetime gift tax exemption, meaning that an individual can make cumulative gifts totaling \$1,000,000 before any gift tax will be payable. With respect to the annual exclusion amount, in 2009, every U.S. person is permitted to gift up to \$13,000 (\$26,000 for married couples) in cash or other assets to as many people as desired each calendar year without any gift tax consequences. In addition to the lifetime gift tax exemption and the annual exclusion amount, it should also be noted that qualified medical and tuition payments can also be made to an unlimited number of beneficiaries without gift tax.

The lifetime gifting opportunities discussed above are some of the simplest and most effective ways of reducing one's taxable estate without incurring any wealth transfer taxes and should be considered as part of any estate plan.

9. Charitable Giving can be Smart Estate Planning.

In addition to the altruistic and goodwill benefits of any charitable contribution, charitable giving may provide significant estate and gift tax benefits. For example, a charitable remainder trust (CRT) is an irrevocable trust that provides for the specific distribution, at least annually, to one or more noncharitable beneficiaries for a term of not more than 20 years. The remainder interest must be transferred to or for the benefit of a qualified charity. Because a CRT is generally exempt from income tax, a grantor can fund a CRT with appreciated property and the CRT will not recognize gain on the subsequent sale of the property. This allows the grantor to dispose of the property without recognizing any capital gain, which, in turn, enables the grantor to generate a higher income stream than would be possible without a CRT. In addition, upon

the creation and funding of a CRT, the grantor is entitled to a charitable contribution deduction equal to the present value of the remainder interest.

10. Everything Discussed Above is Just the Tip of the Iceberg.

In addition to some of the planning techniques discussed above, a myriad of strategies, both conservative and aggressive, are regularly used to

remove the value of assets from your taxable estate, or at the very least “freeze” the value of such assets for estate tax purposes. Some of the more commonly used estate planning strategies include the use of qualified personal residence trusts (QPRTs), family limited partnerships (FLPs), self-cancelling installment notes (SCINs) and grantor retained annuity trusts (GRATs), all of which yield significant estate tax savings if properly structured. ■

Andrew M. Berger is an attorney in the Corporate, Tax, & Securities Law Practice Group of Becker & Poliakoff, P.A. He can be contacted at 954-364-6074 or aberger@becker-poliakoff.com.