BETTER ESTATE PLANNING

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Changes you may have experienced in recent years can impact your immediate and long-term financial and estate planning.

Examples include fluctuations in the value of real estate, stocks and other investments, low interest rates, more Americans retiring each year and variations in the makeup of families.

Whether or not you have experienced some or all of these, one change that will affect a large number of estate plans is the elimination of the federal estate and gift tax for the vast majority of Americans.

As a result, many will be revisiting their estate plans and may find that with no tax liability expected, they can plan their affairs with more freedom.

Some may find that funds that would have been used to pay estate taxes previously will now be available to leave to loved ones. At the same time, additional funds will be available to make charitable gifts.

A practical approach to planning

Having an organized approach to estate planning can make an overwhelming task simpler. A good approach is to focus your attention on four things: the *people* in your life, the *property* you own, your *plans* for the future and the *planners* who will assist you in meeting your goals.

People: List the individuals for whom you would like to provide, beginning with yourself, your spouse, children, parents and others. You may want to include one or more charitable interests in this list as well.

Property: Next, make a list of the property you own or expect to own in the future. Include bank accounts, real estate, stocks, bonds, mutual funds, the value of life insurance policies and their expected proceeds, retirement plan balances and personal property. Beside each item, note the original cost and estimate its current value.

At this point, you should also make a list of sources of income and any outstanding liabilities, such as mortgages and other debts.

Plans: Think about what you wish to accomplish financially over the remainder of your life. Do you anticipate having adequate income to support yourself and others who may depend on you? Who would you like to inherit your property when you no longer need it?

Would you like for heirs to receive property, an income or both? At what ages? Will a trust or other special plans be necessary in order to carry out your wishes? Have tax law changes affected your plans?

Planners: To ensure your estate plan fits your needs, the assistance of one or more advisors will usually be necessary, such as your attorney, accountant or a trust officer.

Others, such as financial planners, investment advisors, life insurance and real estate professionals and similar specialists may also be needed to implement your plans.

Make a list of your primary advisors. Consider one you trust to coordinate the process.

Estate planning tools

After you have given careful thought to the people in your life, your property, your plans and the planners who will assist you, it is time to set your plans in motion.

Your planners can help you explore the advantages of using one or more of the following estate planning tools as part of your long-range plans.

The will as a cornerstone

A well-planned will is normally at the center of an estate plan. While there are other ways to transfer various types of property, people typically rely on a will to:

- Distribute property not transferred through joint ownership, insurance policies, retirement plans, trusts or other arrangements.
- Determine ownership of property that may be acquired in the future.
- Allocate assets that may be converted to other forms over time.
- Back up any trusts or other plans that may no longer be in existence.

In addition to distributing property, a will can be used to recommend guardians for minor children, when necessary. You can also make provisions for the management of assets should an heir be unable to manage property left to them due to age or other factors.

Trusts for asset management

In addition to a will, various types of trusts can be created to help provide for the management and distribution of property under special circumstances.

As the name implies, a “trust” allows you to entrust property to a person or institution and includes your instructions to manage it on behalf of one or more people for a period of time you determine.

At the end of that period, the trust terminates and its assets are divided as you directed when the trust was created.

Trusts are often established to manage funds for those who are disabled, elderly or young enough to require assistance for a time until they can responsibly manage property.

In the case of a *revocable living trust*, you and/or others may serve as trustee of your property for a time, with someone else appointed to take over management of assets, if necessary. Such a trust is called a "living" trust because it is established during your lifetime. It is "revocable" because you may choose to change or end the trust at any time.

A revocable living trust, when used alongside a will, can sometimes reduce the cost and delay of the probate process as a court will not normally need to determine how the trust assets are eventually delivered to loved ones and others.

Power of attorney

Through a properly drafted *power of attorney*, you appoint someone you trust to oversee your property and handle certain other financial affairs on your behalf if you are temporarily or permanently unable to manage your affairs. Your attorney can provide details.

Joint ownership

Homes, automobiles, bank and investment accounts and certain other types of property may be owned jointly with others.

At the death of one owner, the property can pass outside of probate to the surviving owner(s). There are various types of joint ownership, so be sure to choose the one best suited to your needs. Remember, a will does not generally affect the future ownership of jointly held property.

Beneficiary designations

Remember to check the beneficiary designations on any insurance policies or retirement plans to make sure they are current. The terms of a will may not affect their eventual distribution. Provisions similar to beneficiary designations are available in several states for bank and investment accounts.

A living will

A *living will* makes your health care wishes known to your physician and others and can be important in guiding loved ones when making decisions regarding medical care. Check with your advisors about the laws regarding living wills in your state.

Not to plan *is* to plan

What if you decide not to make an estate plan? In that event, a state court will step in and apply an all-purpose "will." The state's standard plan will typically result in the following:

- Someone you do not know may be appointed to settle your affairs.
- The state will direct this person to dispense your property according to state law, which treats family members equally based on their relationship to you, regardless of individual need.
- If you are survived by minor children, a court will appoint their guardian.
- There will be no one granted access to protect your digital accounts.
- Gifts to friends or charity will not be considered, regardless of your friendships or philanthropic interests during your lifetime.

Those who have experienced the results of a "state-made plan" would agree it is much better to make your own plans. See your advisors for more information about the laws of your state. They can assist you in planning for the current and future management and disposition of your property.

The charitable dimension

In recent years growing numbers of people enjoy making gifts to charity. But out of necessity, their own economic security and that of their loved ones must come first.

Because of this you may wish to consider making charitable gifts through your estate plans from what remains after you have first provided for yourself and others. This can be accomplished with a gift through your will, a revocable living trust gift, a beneficiary designation of life insurance or retirement plan proceeds or a number of other convenient planning opportunities.

Through effective estate planning you can also make charitable gifts featuring income, current and future tax savings and other important financial benefits.

Income and asset management

For example, certain charitable gift planning tools offer management of assets for you and/or others while providing a fixed or variable income for life or other period of time. At the end of the time period you determine, the assets are then devoted to charitable use.

Potential tax savings

You can enjoy substantial income, capital gain, gift and estate tax savings through the use of these charitable gift planning techniques.

Generous income tax deductions are allowed for gifts completed during one's lifetime, and assets that will eventually pass to charity can help reduce or eliminate state or federal estate taxes that might otherwise be due.

Because of tax law changes in recent years, many people will experience lower federal taxes on their estates, making more assets available for loved ones and charitable gifts.

Income for life

An example: John Williams, age 78, is concerned about reduced income from a portion of his investment assets. His sister Grace, age 75, lives with him, and he helps support her financially.

Through a carefully planned charitable gift, John learns that he can provide an additional source of income for them for the rest of their lives. This gift plan results in immediate tax savings and also allows for professional management of assets.

A charity they both support will receive the remainder of the assets following their lifetimes. To summarize, John enjoys:

- Fixed or variable income for life for him and his sister.
- Responsible management of assets.
- An immediate income tax deduction that can be used to reduce income taxes for up to six years.
- No capital gains taxes at the time the gift is made.
- Reduction or elimination of estate taxes that might otherwise be due.
- The knowledge that remaining assets will eventually be used to further his charitable interests.

Arranging a temporary gift

Did you know you can also make gifts that provide immediate funding for charitable purposes for a period of time before benefiting your loved ones?

You can set aside assets in a *charitable lead trust* to accomplish this goal. Payments from this type of trust are devoted to charitable purposes for the time period you choose. The assets are then returned to others you designate.

This method can be used to fund a meaningful gift over time while reducing or completely eliminating state and/or federal gift and estate taxes that might otherwise be due on assets when received by your children, grandchildren or other loved ones.

A lead trust can temporarily delay an inheritance in a way that helps reduce estate and gift taxes while also funding charitable gifts.

A number of possibilities

As you can see, balancing your needs with those of loved ones and charitable interests can lead to welcome benefits for all.

Additional information about charitable estate and gift planning is available upon request. The technical advisory section that follows may be of particular interest to your advisors as you make your plans.

Technical Advisory Section

The preceding pages are intended as a general guide to help you as you consider your estate plans. The following information and references to other resources may be beneficial to you and those who assist you in your estate and financial planning.

Federal gift and estate tax considerations

The *Tax Cuts and Jobs Act of 2017* continued the trend toward reducing the impact of federal estate and gift taxes on personal estate planning. The federal estate and gift tax rate is 40% for assets valued at more than the exemption amount. On account of federal estate tax law changes in recent years, fewer estates will be subject to estate tax. The amount that can be left to heirs free of federal estate and gift taxes has been increased to $11.58 million for single individuals and $23.16 million for married couples for 2020. This amount will be adjusted for inflation in future years. Check for latest amounts.

An unlimited amount of charitable gifts may be deducted from federal estate and gift taxes. See Internal Revenue Code section 2055(a). Check applicable state laws for restrictions that may apply.

The reduction of estate and gift taxes at the federal level on amounts left to family and other loved ones may now mean that more is available to make charitable gifts during lifetime and at death by those who are charitably inclined.

The federal gift tax was reunified with the estate tax by legislation enacted in 2011. The maximum amount that can be given to noncharitable recipients during life was increased in 2011 from $1 million under prior law to the same amount exempt from estate tax (see above). The gift and estate tax exemption is also portable between spouses, meaning that a surviving spouse can elect to use any portion of the estate and gift tax exemption not used by the predeceasing spouse.

For those still subject to federal estate and gift tax, it continues to be possible to transfer unlimited amounts to a spouse during one's lifetime and at death. With proper planning it remains unnecessary for married couples to pay estate tax at the death of the first spouse.

The $11.58 million exemption (as adjusted for inflation) is "portable" between spouses, making it possible for a surviving spouse to use any portion of the exemption not used by the first spouse to die. This can make it possible for a married couple to pass a combined total of $23.16 million (indexed for inflation) free of federal estate and gift tax, without the use of trusts and other complex planning devices.

As a result of the 2017 tax law revisions, the process of estate planning will assume new dimensions and many will want to make significant revisions in their plans. Some people will want to take into account the possibility that federal estate taxes may again be imposed on their estates at a future date or that various states may choose to change their estate tax laws.

Planning tools that help transfer assets in a tax-effective manner to loved ones and charitable interests during lifetime rather than at death may assume even greater importance than in the past. These plans can make it possible in some cases to increase the amount of property that can be transferred under gift and estate tax exemptions.

Annual gift exclusion: An individual can give up to a certain amount each year to as many other persons as they wish without having to pay tax on the gifts (IRC section 2503(b)). For many years, the annual gift exclusion amount was $10,000. Since 1999, however, it has been indexed for inflation. In 2018 the amount was raised to $15,000. Check for the current amount before completing gifts. The annual gift exclusion, however, is available only with respect to gifts of present interests.

Charitable gifts and bequests: In general, any amount can be given to a qualified charity during life or at death free of federal gift and estate taxes because of the unlimited gift and estate tax charitable deductions (IRC sections 2055 and 2522).

In the case of an outright donation in excess of the annual exclusion amount, the first portion of the gift qualifies for the annual gift exclusion under IRC section 2503(b); the balance of the gift qualifies for the gift tax charitable deduction.

Example 1: Mrs. Taylor wishes to leave $25,000 by will to a charitable organization. Rather than leaving the bequest directly to the charity, she includes the $25,000 in the amount she leaves to her husband (tax free under the marital deduction).

Mr. Taylor then voluntarily gives the $25,000 to the organization—saving personal income taxes.

This plan can work well when both spouses share the same charitable objectives because it provides both estate and income tax savings.

Example 2: Mr. Smith wants to establish a trust under his will to provide an income to his wife for her life. He and his wife agree that the remainder interest in the trust should go to a shared charitable interest.

Mr. Smith's will can establish, for example, either a QTIP trust with a charitable remainder (IRC section 2056(b)(7)) or a qualified charitable remainder annuity trust or unitrust, as defined in IRC section 664.

In either case, assuming all applicable requirements are met, the assets left to the trust will be free from estate tax at both Mr. and Mrs. Smith's deaths because of the unlimited marital and charitable deductions. See IRC sections 2523(a) and 2056(a).

Charitable remainder trusts: The charitable remainder annuity trust or unitrust, on the other hand, would provide Mrs. Smith with either (1) a fixed annuity type of payout or (2) a payout equal to a fixed percentage of the annually determined asset value of the trust. Apart from the annual payout, Mrs. Smith could not receive any amounts of trust income or principal.

Applicable law provides for a minimum payment of 5%, a maximum payout rate of 50% and a 10% minimum charitable remainder amount for charitable remainder trusts. Particular care should be given to drafting provisions of testamentary charitable remainder trusts.

Generation skipping transfer (GST) tax: This area of the law is quite complicated; however, charitable gifts may minimize the amount of transfer tax owed for some estates. It is one consideration to explore if the support of future generations is one of the person's goals and if the estate would otherwise be affected by the generation skipping transfer tax. Under terms of federal tax legislation in 2017, the amount exempt from the GST tax was also increased to $11.58 million per individual for 2020.

For details on the GST tax, see Code sections 2601–2663 and the corresponding regulations, and check for the latest changes in the law governing this provision.

Charitable lead trusts: A charitable lead trust makes an annuity or unitrust payout to a qualified charitable organization for a specified term of years (or for a life or lives) and then distributes its assets, typically to the donor's children or grandchildren (see IRC sections 2055(e)(2)(B), 2522(c)(2)(B)).

The initial present value of the charitable payout qualifies for the gift or estate tax charitable deduction, as the case may be. The taxable transfer to the heirs, therefore, is equal to the difference between the amount given to the trust and this present value.

For a person who has a large estate—especially an unmarried individual who cannot take advantage of the marital deduction—the lead trust is often an option that offers welcome opportunities to reduce or eliminate estate and gift taxes that may still apply since estate tax law changes in recent years.

Power of attorney: In some cases, a donor has established a plan of regularly making charitable gifts. If asked, the donor might reply that they would like the plan to continue in the event they become incapacitated.

If this is the person's wish, assuming they create a durable general power of attorney, an express provision should be included directing the attorney-in-fact as to the specifics of making contributions out of the donor's assets.

Conclusion

There are of course more technical considerations to estate and gift planning than those covered in this technical advisory section. Check for recent changes in state and federal law before finalizing estate and financial plans.

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