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ESTATE PLANNING MEMORANDUM

A Client's individual preferences always have primary consideration in an estate planning process. The ultimate goal of estate planning is to provide effective asset protection and tax planning, while meeting the personal needs of the individual. In effect, you want to protect your interests in this life and in the next.

Estate planning involves more than simply drafting a will. It includes tax planning and can encompass lifetime gift arrangements, charitable gift arrangements, life insurance and other kinds of trusts, general durable powers of attorney, living wills, health care proxies and other documents and planning as well.

1. Durable Powers of Attorney

Absent advance planning, if an individual were to become unable to manage his or her affairs because of mental or physical disabilities, his or her family would, have to seek court permission to carry out legal transactions on behalf of the disabled person. With proper advance planning, you can avoid this time-consuming and expensive process. For example, by having a **Durable General Power of Attorney**, appointing another as agent to carry out transactions in the event of disability, you may be able to avoid costly intervention. A well-drafted Power of Attorney should contain some HIPAA Disclosure Language.

2. Living Wills, Health Care Proxies and Appointment for Disposition of Remains

An **Advance Directive** or **Living Will** is a document, which authorizes termination of life support systems in cases in which a person is in persistent vegetative state or is terminally ill and there is no reasonable prospect of recovery. Unless an individual signs such a written document setting forth his or her wishes a facility may be legally obligated to maintain artificial life support systems. Under these circumstances when the quality of life is small or non-existent, many people prefer that medical aid be terminated and the person be allowed to die a peaceful death. A Living Will makes clear one's wishes in this respect. The decision to sign a Living Will is a very personal one, but it is something that should be considered in the estate planning process. A Living Will can be tailored to reflect each client's particular wishes. The authority to terminate medical treatment is usually placed in the hands of a family member through a companion document to the Living Will called a **Health Care Proxy**. A Health Care Proxy allows you to appoint another person to make all medical decisions, both routine and end of life, for you, when you are unable to communicate with the doctor. A well-drafted Health Care Proxy should contain some HIPAA Disclosure Language. The authority to take possession of the person's remains is usually placed in the hands of the next-of-kin governed under State Law. If the individual's next-of-kin differs from the person he/she wishes to take possession of his/her remains and insure that the person's last wishes as to the disposition of their remains is carried out, an individual needs to designate an agent to carry out these instructions. An **Appointment for Disposition of Remains** can reference the type of disposition (for example, cremation) as well as if pre-need arrangements have been acquired.

3. Last Will & Testament

A **Will** allows a person to exercise his or her wishes regarding the distributions of assets after death. A Will affects only property owned by a person at death, which does not transfer automatically to another individual by operation of law, such as joint tenancy with right of survivorship or by a specific designation such as with life insurance, by not having a Will, an individual's assets go according to state law. Through a process called intestacy, the state will determine the distribution of assets, select the estate administrator and tax planning, opportunities may be lost. Having a properly drafted Will can provide the person with peace of mind and ensure that your wishes govern how your estate will be administered.

4. Living Trusts

A **Living Trust** is a trust created during one's lifetime and can generally be revoked at any time prior to death unless provided otherwise. The primary benefit of a Living Trust is avoidance of the probate process. All assets in the trust at death pass automatically to the beneficiaries named in the trust. A further advantage of a Living Trust is the uninterrupted management of the assets upon incapacity of the grantor of the trust. The Trustee of the trust will continue to manage the affairs of the trust without the necessity of court intervention. A Living Trust acts as a more comprehensive Durable Power of Attorney. In many situations, a Living Trust is an excellent asset protection vehicle by allowing a Trustee to take the necessary measures to preserve assets.

Trusts can be structured as Asset Protection vehicles. "**Spray**" trusts where the trustee has the discretion to distribute or accumulate income or principal amongst a class of beneficiaries protects against creditors of the beneficiaries.

Trusts can be structured where *distributions are frozen upon the occurrence of a triggering event* such as substance abuse, divorce, or gambling addiction. Once the beneficiary has been free of the triggering event for a term (this author provides for free of socially unacceptable behavior for a period of three years), the trustee has the discretion to commence distributions again.

Supplemental Needs Trusts (SNTs) are classic asset protection vehicles. The SNT is created where an individual who is (or may be) on Government Assistance can have funds set aside for them to supplement their care but the funds are not viewed as "available resources" making them ineligible to receive assistance.

5. Marital deduction

One spouse can give to the other an unlimited amount of property during lifetime or at death without any federal estate or gift tax consequences. The availability of the unlimited marital deduction normally means that the payment of the estate taxes can be deferred until the death of the survivor of a husband and wife. Without special planning, however, the unlimited marital deduction is not available to a non-citizen spouse, even though he or she may have resided in the United States for decades. Please note that with special planning, the non-citizen spouse can be provided for.

A disposition to a surviving spouse can be wholly or partly in trust rather than outright, so that the Will of the first spouse to die can control the ultimate disposition of the marital deduction funds, with the surviving spouse being entitled to all of the income earned on the funds during his or her lifetime, and with the principal being available for him or her in the discretion of the trustees. The use of a marital deduction trust can provide assurance that the children of the marriage ultimately will receive an inheritance from the first spouse to die, regardless of any other considerations, such as whether the surviving spouse is financially unsophisticated, remarries and/or has a new family after the first spouse's death.

6. Applicable credit

Every individual has available an “applicable credit”, to use against lifetime gifts or at death, which will permit property of certain value to be transferred without tax this year.

The exemptions and maximum federal estate tax rates are shown below:

| <u>Year</u> | <u>Maximum Estate Tax Rate</u> | <u>Applicable credit</u> |
|-------------|--------------------------------|--------------------------------|
| 2008 | 45% | \$2,000,000 |
| 2009 | 45% | \$3,500,000 |
| 2010 | 35% or 0% | \$5,000,000 (if not elect out) |
| 2011 | 35% | \$5,000,000 |
| 2012 | 35% | \$5,120,000 |
| 2013 | 40% | \$5,250,000 |

An estate plan should maximize utilization of the applicable credit amount to produce the best estate tax savings posture. The NYS estate credit has remained at \$1,000,000.00.

If, as is often the case, the applicable credit is not fully used through lifetime giving, it makes sense for the Will of the first spouse to die to create a trust to “carve out” and hold the applicable credit amount. Effective use of the applicable credit in both estates of a husband and wife can be quite significant, resulting in as much as \$10,500,000 (for year 2013) in combined assets of the couple passing to their children without federal estate taxation, and ultimately reducing estates taxes on assets passing to the couple’s children.

Beginning January 1, 2011, estates of decedents survived by a spouse may elect to pass any of the decedent’s unused exemption to the surviving spouse. This election is made on a timely filed estate tax return for the decedent with a surviving spouse. Note that simplified valuation provisions apply for those estates without a filing requirement absent the **portability** election.

Will planning in this area involves the creation of what is commonly called a “credit shelter trust” or “by-pass trust”. The individual’s Will “carves out” from the gross estate the amount that can be protected by the available applicable credit amount and provides that this amount will not pass outright to the surviving spouse, but rather will be held in the trust created by the Will for the benefit of the surviving spouse (and, depending on the overall assets available, perhaps for the children) during the surviving spouse’s lifetime. The trustee can be given the power to use trust principal for the trust beneficiaries as well. On the death of the surviving spouse, the trust can terminate and pay out directly to children, or the assets can continue to be held in trust for the benefit of the children until they reach desired ages. To add flexibility, Wills may provide for a “disclaimer credit shelter trust” by which the surviving spouse would have nine months from the first spouse’s death to disclaim either a fixed dollar amount or a percentage of the surviving spouse’s interest as a beneficiary in the deceased spouse’s estate. Any disclaimed property would pass to a trust created by the Will. This technique provides the surviving spouse with the ability to make post-death tax

planning decisions and can be especially useful in Wills of a married couple who may not, at the time the Wills are signed, have sufficient assets to utilize effectively a by-pass trust but who may be able to use the estate tax savings benefits from such a trust in the future. Disclaimed assets would be subject to estate tax in the estate of the first spouse to die, thereby permitting utilization of the credit amount in the first estate.

7. Annual Exclusion

The tax law permits every individual to give \$14,000 per year to as many persons as he or she wishes (\$28,000 for each recipient for married donors), without gift tax consequences. The transfer must be a transfer of a present interest. Tuition costs paid directly to an educational institution and medical expenses paid directly to a care provider are not subject to federal gift tax, regardless of the amounts involved and are an addition to the annual exclusion amount. For individuals who are in the position to make annual exclusion gifts on a regular basis, the amount that can be removed from one's estate over time without wealth transfer tax consequences can be quite substantial. The annual exclusion is indexed by inflation.

8. Beneficiary Designations

It is important to the estate planning process that all beneficiary designations under life insurance contracts, IRA qualified funds and the like be reviewed to be sure that the beneficiary designations work according to the individual's wishes. There should always be contingent beneficiaries named in case the primary beneficiary predeceases the individual.

9. Title to Assets

The manner in which spouses hold title to assets is important to the overall effectiveness of an estate plan. Jointly held assets pass automatically to the surviving joint tenant outright and do not pass under one's Will. This is often the case with a couple's home, bank accounts, and sometimes with portfolio investments. Other assets have the same result, such as assets passing by beneficiary designations, including life insurance proceeds and retirement plan proceeds. While these assets are taken into account in the taxing process, they do not pass under, and are not governed by the individual's Will. It is important, therefore, to consider how title to assets is held.

This information is for educational purposes only. By reviewing this material you will be more informed when dealing with an attorney chosen to create your estate plan. After reviewing this material, please call my office to set up a consultation. During this consultation, I will review your existing documents and determine the appropriate estate plan for your individual needs.