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What you need to know about Estate Planning

I hope you find our eCommunications to be helpful, educational, informative, and worthwhile. Contact us if you have questions or concerns as they relate to your specific circumstances or would like to discuss any of these topics in greater detail. We welcome your calls and feedback. To save time, try our Calendar Link to schedule a convenient time. During these unprecedented times, many folks are seeking professional guidance. Feel free to share this information with friends, family, associates, and others who can benefit or may seek professional help or advice from a seasoned veteran who has weathered numerous Black Swan events. We look forward to being a resource and being available to help guide you through these treacherous times.

Very best regards,

John M. Sklencar, RFC

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Introduction to Estate Planning

What is estate planning?

Simply stated, estate planning is a method for determining how to distribute your property during your life and at your death. It is the process of developing and implementing a master plan that facilitates the distribution of your property after your death and according to your goals and objectives.

At your death, you leave behind the people that you love and all your worldly goods. Without advance planning, you have no say about who gets what, and more of your property may go to others, like the federal government, instead of your loved ones. If you care about (1) how and to whom your property is distributed, and (2) ensuring that your property is preserved for your loved ones, you need to know more about estate planning.

As a process, estate planning requires a little effort on your part. First, you'll want to come to terms with dying, at least to a degree that you can deal with the necessary planning. Understandably, your death can be a very uncomfortable subject, but unfortunately, the discussions in this area are full of references to your death, so it really can't be avoided. Some statements may seem too businesslike and unfeeling, but tiptoeing around the subject of dying will only make the planning process more difficult. You will understand the process more easily and implement a more successful master plan if you approach it in a straightforward manner.

Who needs estate planning?

Not just for the wealthy

Estate planning may be important to individuals with a wide range of financial situations. In fact, it may be more important if you have a smaller estate because the final expenses will have a much greater impact on your estate. Wasting even a single asset may cause your loved ones to suffer from a lack of financial resources.

Your master plan can consist of strategies that are simple and inexpensive to implement (e.g., a will or life insurance). If your estate is larger, the estate planning process can be more complex and expensive.

Implementing most strategies will probably require you to hire professional help of some kind, an attorney, an accountant, a trust officer, or an insurance agent, for example. If your estate is large or complex, you should consult with an estate planning expert such as a tax attorney or financial planner for advice before the implementation stage.

In deciding on your course of action, you should always consider whether the benefit of the strategy outweighs the cost of its implementation.

May be especially needed under certain circumstances

You may need to plan your estate especially if:

- Your estate is valued at more than the federal gift and estate tax applicable exclusion amount or your state's death tax exclusion amount
- Your income tax bracket is in excess of 10 percent
- You have children who are minors or who have special needs
- Your spouse is uncomfortable with or incapable of handling financial matters
- You're a business owner
- You have property in more than one state
- You intend to contribute to charity
- You have special property, such as artwork or collectibles
- You have strong feelings about health-care decisions
- You have privacy concerns or want to avoid probate

How to do it

Designing a plan is a process that is unique to each estate owner. Don't be intimidated or overwhelmed at the prospect. Even the most complex plan can be achieved if you proceed step by step. Remember, the peace of mind that comes with developing a successful estate plan is worth the time, trouble, and expense.

Understand your particular circumstances

Begin the estate planning process by understanding your particular circumstances, such as your age, health, wealth, etc.

Understand the factors that will affect your estate

You will also need to have some understanding of the factors that may affect the distribution of your estate, such as taxes, probate, liquidity, and incapacity.

Clarify your goals and objectives

When your particular circumstances and the factors that may affect your estate are clear, your goals and objectives should come into focus.

Understand the strategies that are available

With these goals and objectives now clear, you can begin to consider the different estate planning strategies that are available to you.

Seek professional help

Seeking professional help (an attorney or financial advisor) will help you understand the strategies that are available and formulate and implement your master plan.

Formulate and implement a plan

Finally, after following these steps, you can formulate and implement a plan that works for you. Here are a few basic tips: (1) make sure you understand your plan, (2) rely on people you trust, and (3) keep your documents and information organized and within easy reach.

Perform periodic reviews

When you have implemented your master plan, be sure to perform a periodic review and, if necessary, make revisions that reflect any changing circumstances and tax laws.

How do you begin?

There are many estate planning strategies, including some that are implemented inter vivos (during life), such as making gifts, and others post-mortem (after death), such as disclaimers. Before you choose which strategies are right for you, you need to understand your particular circumstances.

Gather and analyze the facts

Understanding your particular circumstances results from gathering and analyzing the facts. The following questions may help you to accomplish this. If they are not easy to answer, you may have to make some estimates based on reasonable assumptions and expectations.

Information regarding your financial condition

- What is your current income?
- What is your income likely to be in the future?
- How much do you spend each year?
- What are your expenses likely to be in the future?
- What are your current assets and debts?
- Are your assets currently owned solely or jointly?
- What estate planning strategies have you already implemented?

Family information

- Who are the family members you intend to benefit?
- What are the needs of each family member?

What other factors need to be considered?

Decide what your goals and objectives are in light of your particular circumstances and in light of the factors that may affect your estate. The primary factors that may affect your estate are your beneficiaries, taxes, probate, liquidity, and incapacity.

Taxes

One of the largest potential expenses your estate may have to pay is taxes, which may include federal transfer taxes, state death taxes, and federal income taxes.

Federal transfer taxes — The federal transfer taxes include (1) the federal gift tax and estate tax and (2) the federal generation-skipping transfer (GST) tax.

- Federal gift tax — Gift tax is imposed on property you transfer to others while you are living. You need a basic understanding of how the gift tax system works to minimize gift tax liability. Under the gift tax system, in 2020 you are allowed a $11,580,000 lifetime applicable exclusion amount that reduces your gift and estate tax liability (any (basic) applicable exclusion amount you use during life effectively reduces the amount that will be available at your death). Also, you are currently allowed to give $15,000 per donee gift tax free under the annual gift tax exclusion (the annual gift tax exclusion is indexed for inflation, so this amount may change in future years). Further, certain other types of transfers can be made gift tax free. You need to understand what these types of transfer are and how they work to take full advantage of them.

- Federal estate tax — Generally speaking, estate tax is imposed on property you transfer to others at the time of your death. You need a basic understanding of how the estate tax system works for several reasons:
  - Saving your property for your beneficiaries — Estate tax rates could reach as high as 40 percent in 2020, which means that a large chunk of your estate may go to the federal government instead of your beneficiaries. If you want to preserve your estate for your beneficiaries, you'll need to know how to minimize estate tax with respect to your property.
  - Reducing estate tax liability — Under the estate tax system, you are allowed an applicable exclusion amount that reduces your estate tax liability. Also, there are exclusions, deductions, and other credits available that allow you to pass a certain amount of your estate tax free. You need to understand what these exclusions, deductions, and credits are and how they work to take full advantage of them.
  - Providing for the payment of estate tax — Generally, estate tax must be paid within nine months after your death. To avoid depriving your beneficiaries of what you intend for them to receive, you should provide that specific and sufficient assets be set aside and used for this purpose. In addition, these assets should be sufficiently liquid to pay these expenses when they are due.
  - Planning for estate tax expense — Although calculating estate tax can be complex, you should estimate what the amount of your estate tax may be (if any), so that you can arrange to replace that wealth.
- GST tax — Another federal transfer you need to understand is the federal generation-skipping transfer (GST) tax. The GST tax is imposed on property you transfer to an individual who is two or more generations below you (e.g., a grandchild or great-nephew). Not surprisingly, the IRS wants to levy a tax on property as it is passed from generation to generation at each and every level. The purpose of the GST tax is to keep individuals from avoiding estate tax by skipping an intermediate generation. A flat tax rate equal to the highest estate tax then in effect is imposed on every generation-skipping transfer you make over a certain amount. You are allowed a GST tax exemption of $11,580,000 in 2020. Currently, some states also impose their own GST tax. Check with an attorney or your state to find out what may be subject to your state's GST tax, and how and when to file a state GST tax return.

State death taxes — States also impose their own death taxes. You should be aware of what the death tax laws are in your state and how they may affect your estate. There are three types of state death taxes: (1) estate tax, (2) inheritance tax, and (3) credit estate tax (also called a sponge tax or pickup tax). Some states also impose their own gift tax and/or generation skipping transfer tax.

- Estate tax — State estate tax is imposed on property you transfer to others at your death, much like federal estate tax. The state estate tax calculation for most states is similar to the federal calculation.
- Inheritance tax — Unlike estate tax, the inheritance tax is imposed on your beneficiary's right to receive your property. Tax is due on each beneficiary's share of your estate. Beneficiaries are grouped into classes (generally based upon their familial relationship to you) and are taxed accordingly. Although inheritance tax is due on each heir's share of your estate, it's your personal representative who writes the check from your estate to pay it.
- Credit estate tax — Some states impose a credit estate tax (also referred to as a sponge tax or pickup tax).

Tip: *Most states that imposed a credit estate tax have "decoupled" from the federal system (i.e., they're imposing some form of stand-alone estate tax.)*

Tip: *The federal system allows a deduction for state death taxes for the estates of persons dying in 2005 and later. Prior to 2005, a credit was available.*

Federal income taxes — In the estate planning context, you should be aware of three federal income tax considerations:

1. Income taxation of trusts — If your estate plan includes the use of a trust, you need to know that a trust may be an income tax-paying entity. The trustee may be required to file an annual return and pay income taxes on trust income.
2. Decedent's final income tax return — Your personal representative or surviving spouse has the duty of filing your last income tax return that covers the tax year ending on the date of your death.
3. Income taxation of your estate — Your estate is considered a separate income taxpaying entity. Your personal representative must file and pay income taxes on any income your estate receives (e.g., interest from bonds, or dividends from stock).

Probate

Probate is the court-supervised process of proving, allowing, and administering your will. The probate process can be time-consuming, expensive, and open to public scrutiny. Avoiding probate may be one of your most important goals. To develop a successful avoidance strategy, you'll need to understand how the probate process works, how to estimate probate costs, and what is subject to probate.

Liquidity

Estate liquidity refers to the ability of your estate to pay taxes and other costs that arise after your death from cash and cash alternatives. If your property is mostly nonliquid (e.g., real estate, business interests), your estate may be forced to sell assets to meet its obligations as they become due. This could result in an economic loss, or your family selling assets that you intended for them to keep. Therefore, planning for estate liquidity should be one of your most important estate planning objectives.

Incapacity

Planning for incapacity is a vital yet often overlooked aspect of estate planning. Who will manage your property for you when you can no longer handle these responsibilities? You need to ask and answer this question because the consequences of being unprepared may have a devastating effect on your estate and loved ones. You should include plans for incapacity as a part of your overall estate plan.

What are your goals and objectives?

Your goals and objectives are personal, but you can't formulate a successful plan without a clear and precise understanding of what they are. They can be based on your particular circumstances and the factors that may affect your estate, as discussed earlier, but your feelings and desires are just as important. The following are some goals and objectives you might consider:

- Provide financial security for your family
- Ensure that your property is preserved and passed on to your beneficiaries
- Avoid disputes among family members, business owners, or with third parties (such as the IRS)
- Provide for your children's or grandchildren's education
- Provide for your favorite charity
- Maintain control over or ensure the competent management of your property in case of incapacity
- Minimize estate taxes and other costs
- Avoid probate
- Provide adequate liquidity for the settlement of your estate
- Transfer ownership of your business to your beneficiaries

What are estate planning strategies?

An estate planning strategy is any method that facilitates the distribution of your assets and the settlement of your estate according to your wishes. There are several estate planning strategies available to you.

Intestate succession

Intestate succession is a strategy by default and is a means of transferring your property to your heirs if you have failed to make other plans such as a will or trust. State law controls how and to whom your property is distributed, who administers your estate, and who takes care of your minor children. Without directions, your opinions and feelings are not considered. Indeed, one of your primary goals in planning your estate may be to avoid intestate succession.

Last will and testament

A will is a legal document that lets you state how you want your property distributed after you die, who shall administer your estate, and who will care for your minor children. This is probably the most important tool available to you. Anyone with property or minor children should have a will.

Will substitutes

A will substitute, for example, Totten Trust and payable on death bank accounts, allows you to designate a beneficiary of certain property that will automatically pass to that beneficiary after you die and avoids passing through probate.

Trusts

A trust is a separate legal entity that holds your assets that are then used for the benefit of one or more people (e.g., you, your spouse, or your children). There are different types of trusts, each serving a different purpose, and include marital trusts and charitable trusts. You will need an attorney to create a trust.

Joint ownership

Joint ownership is holding property in concert with one or more persons or entities. There are different types of joint ownership, such as tenancy in common and community property, each with different legal definitions, requirements, and consequences.

Life insurance

Life insurance is a contract under which proceeds are paid to a designated beneficiary at your death. Life insurance plays a part in most estate plans.

Gifts

A gift is a transfer of property, not a bona fide sale, that you make during your life to family, friends, or charity. Making gifts can be personally gratifying as well as an effective estate planning tool.

Tax exclusions, deductions, and credits

There are several important estate planning tools you can use that are offered by the federal government. These include the annual gift tax exclusion, the applicable exclusion amount, the unlimited marital deduction, split gifts, and the charitable deduction.

Wills

What is a will?

A will may be the most vital piece of your estate plan, even if your estate is a modest one. It is a legal document that lets you direct how your property will be dispersed (among other things) when you die. It becomes effective only after your death. It also allows you to nominate an estate executor as the legal representative who carries out your wishes. In addition, in many states, your will is the only legal way you can name a guardian for your minor children.

Without a will, your property will be distributed according to the intestacy laws of your state. The laws of your state also govern the validity of a will.

What are the requirements?

Requirements vary from state to state. Generally, for your will to be valid, the following requirements must be satisfied.

You must be 18 and of sound mind

Generally, you must be 18 years of age to execute a will, although some states have a different minimum age requirement.

You also must be of sound mind. That means that you must have testamentary capacity--that you know and understand what property you own, its nature, who would inherit it, and the plan for disposition outlined in the will. You must also be free of undue influence or fraud at the time the will is drafted. In other words, you must draw up a will of your own free will.

Will must be properly executed

Your will must be properly executed. Generally, this means that the will must be:

- Written--The general rule is that a will must be written. Usually, the will is typewritten or in some printed form. The one exception to the general rule is a nuncupative (oral) will. Nuncupative wills are generally valid only if made during your last illness and only if the witnesses reduce it to writing very soon afterward.
- Signed by you (the testator)--You or someone in your presence and at your direction must sign the will.
- Witnessed--Generally, your signature must be witnessed by two competent persons. Some states require three witnesses and some require no witnesses in certain cases, such as when a holographic will is executed. A holographic will is a will that is valid despite not being witnessed because it is completely in the testator's handwriting. Other states may also require that the signatures be notarized.

Technical Note: *Competency is a legal term. It means that the witnesses are of legal age (generally 18) and understand what they are witnessing. A witness is generally not considered competent if he or she is a beneficiary under the will and would not inherit if you died intestate. If this happens, the state will generally void the devise or legacy to that beneficiary. Some states void bequests to all witnesses.*

What does your will do?

Avoids intestacy

Probably the greatest advantage to a will is that it allows you to avoid intestacy. State intestate succession laws, in effect, provide a will if you fail to do so. This "intestate's will" distributes your property the way the state thinks you would have if you had made a will (i.e., to your spouse or closest blood relatives). However, this may not necessarily be what you would want. Also, intestacy has many other disadvantages (e.g., thwarts tax minimization planning).

Distributes property according to your wishes

With a will, you can leave: (1) a specific bequest (such as jewelry, an heirloom, furniture, or cash), (2) a general bequest (such as a percentage of your property), or (3) your residuary estate (what's left over) to a surviving spouse, a child, another relative, a friend, a trust, a charity, or anyone, according to your wishes.

Caution: *There are some limits imposed on how you can distribute your property with a will (e.g., you cannot completely avoid a spouse's right to inherit).*

Most states will not let you leave property directly to a pet, nor will they let you set up a trust for a pet in the pet's name. However, you can leave money in your will for someone to care for your pet after your death. A more expensive option is to establish a trust in someone's name, and specify in the trust document that the funds are to be used for looking after your pet. Make sure the caretaker agrees in advance to look after your pet.

Nominates a guardian for your minor children

In many states, a will is your only means of stating which individual(s) you wish to act as legal guardian for your minor children after you die.

You can name a guardian of the person, who takes personal custody of the children, and a guardian of the property or estate, who manages the children's assets. This can be the same or a different person.

Caution: *The probate court has final approval, but it will usually approve whomever you nominate unless there are compelling reasons not to do so.*

Nominates an executor

A will allows you to designate a person to act as your legal representative after your death. An executor carries out many estate settlement tasks, including locating and probating your will, collecting your assets, paying legitimate creditor claims, paying any taxes owed by the estate, and distributing any remaining assets to your beneficiaries.

Caution: *The probate court has final approval, but it will usually approve whomever you nominate unless there are compelling reasons not to.*

Specifies how to pay estate taxes and other expenses

Unless you direct otherwise in your will, the beneficiaries will bear liability for estate taxes and other expenses according to state law. To ensure that your beneficiaries receive what you intend for them to have, you can provide in your will that these costs be paid from the residuary estate (what's left over). Or, you can specify which assets should be used or sold to pay these costs.

Creates a testamentary trust

You can create a trust in your will, which comes into being when your will is probated. Your will sets out the terms of the trust, such as who the trustee is, who the beneficiaries are, how the trust is funded, how the distributions should be made, and when the trust terminates.

Tip: *Using a trust may be especially important if you have a spouse or minor children who are unable to manage property themselves.*

Funds a living trust

If you have or plan to establish a living trust (one that is created while you are living), your will can transfer (pourover) any assets that were not already transferred to the trust.

Minimizes taxes

Your will gives you the chance to minimize taxes and other costs.

Example(s): *Ken drafts a will that leaves his entire estate to his wife, Sue. Ken dies. None of Ken's property is taxable because he left it all to his wife, and it is therefore fully deductible under the unlimited marital deduction.*

Are there any tradeoffs?

Although the benefits of a will far outweigh the drawbacks, there are some tradeoffs.

Assets disposed of through a will are subject to probate

Probate (the court-supervised process of administering your will) can be expensive and time-consuming. The length of probate can be affected by several factors including the size and complexity of the estate, any challenges to the will or its provisions, creditor claims against the estate, who your beneficiaries are, state probate laws and the state court system, and tax issues.

Owning property in more than one state can result in multiple probate proceedings. This is called ancillary probate. Generally, real estate is probated in the state in which it is located, and personal property is probated in the state in which you are domiciled (i.e., reside) at the time of your death.

Will provisions can be challenged in court

The validity of your will can be challenged in court. Usually, an unhappy beneficiary or a disinherited heir will present the challenge. Some common claims include:

- You lacked testamentary capacity when you drew up the will
- You were unduly influenced by another individual when you drew up the will
- The will was forged or was otherwise improperly executed
- The will was revoked.

Tip: *You can attempt to discourage challenges to your will by including a "no contest" provision. Stipulate in your will that if beneficiaries try to gain a greater portion of the estate, they will be disinherited entirely. For the "no contest" provision to have any bite, however, you must make a bequest to a beneficiary you expect may contest the will, so that he or she has something to lose by contesting your will. The degree to which "no contest" provisions will be enforced varies by state. A typical provision would look like this: "If any beneficiary should contest the probate or validity of my will, then all benefits for the beneficiary shall cease and this instrument shall be interpreted as if the beneficiary had predeceased me"*

Wills are public documents

Once probated, a will becomes a public document, available to anyone who wishes to read it. This can be discomfiting for anyone who has privacy concerns. Anyone can find out what you have left in your estate and to whom you have left it, thus exposing your beneficiaries to fraud or other crimes. Also, if you make negative or embarrassing statements about a person in your will, you leave your estate vulnerable to a libel suit.

How do you make a will?

Hire an attorney

Although a will need not be drafted by an attorney to be valid, it is highly recommended that you seek an attorney's advice to ensure that your will does what you intend.

Determine what you leave in your will

You must determine whether (1) you can dispose of an asset in your will and (2) whether you should dispose of an asset in your will.

Before you can give away what you own, you must figure out what it is that you own. The way in which you own property will determine whether you can transfer that asset in your will. Solely owned property is property owned by you alone and generally can be transferred by will. Property held in joint tenancy , tenancy by the entirety , and community property , on the other hand, generally passes in whole or in part directly to the joint owner at your death. Property held as joint tenants or tenants by the entirety can't be transferred by will.

Also, remember that property in which you have already named a beneficiary does not pass by your will (e.g., life insurance, pension plans, IRAs, Totten Trust accounts, Payable on Death accounts).

Once you have determined what you can give away in your will, you need to decide if you should. It may be better to dispose of property while you are living , rather than at death. For example, you may want some transfers to remain private or you may want to reduce estate taxes by giving away during your lifetime property that is likely to greatly appreciate (increase in value).

Tell someone your funeral wishes

Because your will might not be read immediately after your death, it may not be possible to have your funeral and burial wishes honored if you include them in your will. Instead, put funeral wishes in a separate letter of instruction; leave the letter with a trusted friend, close relative, or your executor; and have it read immediately upon your death.

Choose your beneficiaries

Beneficiaries are the people and organizations to whom you leave property. They can be relatives, friends, trusts, or charities. The essence of the will-making process revolves around thinking about the property you own and who you want to have it after your death.

Select a guardian for your minor children

If you have minor children, you will want to nominate a guardian in your will to care for them and their property after you die, should their other parent not be able to care for them. This is an extremely important decision.

Select an executor

Your executor is responsible for carrying out the instructions of your will and managing the probate process. This includes locating your will, collecting your assets, paying legitimate creditor claims, paying any taxes owed by the estate, and distributing any remaining assets to your beneficiaries. Choosing an executor is another very important decision.

Draft a will

Each state has its own laws governing the validity of will provisions, the format a will must take, and execution formalities. Here are some tips:

- Include a clause revoking any prior wills and codicils
- Use specific and definite language to avoid questions later about your intent.

Example(s): *"I leave my daughter, Judy, nothing. I intentionally omit Judy from my will, not because I do not love her, but because she is wealthy in her own right and does not need my money."*

- Mention personal effects (especially valuable articles) specifically
- Mention outright cash gifts specifically
- Mention dispositions of real estate specifically
- Make special provisions for any business interests
- Make special provisions for the payment of taxes and other costs
- Consider making special provisions to reduce the amount of specific bequests and legacies in the event that the value of your estate falls below a certain level

Properly execute the will

Your will must be properly executed. Generally, this means that the will must be:

- Written--The general rule is that a will must be written. Usually, the will is typewritten or in some printed form. However, some states allow a holographic (handwritten) will. The one exception to the general rule is a nuncupative (oral) will. Nuncupative wills are generally valid only if made during your last illness and only if the witnesses put it in writing very soon afterward.
- Signed by you (the testator)--You, or someone in your presence and at your direction, must sign the will.
- Witnessed--Generally, your signature must be witnessed by two competent persons. Some states require three witnesses and some don't require any in certain circumstances. Others require that the signatures be notarized.

Technical Note: *Competency is a legal term. It means that the witnesses are of legal age (generally 18) and understand what they are witnessing. A witness is generally not competent if he or she is a beneficiary under the will and would not inherit if you died intestate. If this happens, the state will generally void the devise or legacy to that beneficiary. Some states void bequests to all witnesses, which has the effect of making interested witnesses competent and the will validly witnessed.*

Store the will in a safe, accessible place

Wills should be stored in a secure and accessible place. Your executor and at least one close family member should know where you keep your will. Storage options include a file in your attorney's office or a fireproof safe at home. In some areas, it is possible to keep a copy of your will on file at the local probate court.

Caution: *It is not recommended that you store your will in a bank safe deposit box. Some states seal safe deposit boxes upon the owner's death, and the box can be opened only after obtaining the probate court's approval.*

Review your will annually or upon certain events

A will is not a static document and should be reviewed at least annually or whenever your life situation changes. Here are some circumstances under which you may want to revise your will:

- You marry or remarry
- You have a child
- You divorce
- Your spouse or child dies
- You move to another state
- Your income changes
- You retire
- The value of your estate changes
- Tax laws change

Can you change or revoke your will?

You can amend (change) your will by executing a codicil . A codicil is a separate, written, and formally executed document that becomes part of your will. A codicil generally should be used only for minor changes to your will. You should execute a new will if there are many changes or a major change.

Revoking your will must be done very carefully. If not done correctly, the will remains valid until properly revoked or superseded. Most state laws require that the will be revoked by a subsequent instrument (a new will) or by a physical act (e.g., destroying or defacing it). That means that the will must be either burned, torn, or canceled with the intent to revoke.

Example(s): *Example A: Mary executes a valid will leaving her entire estate to Jason. Mary throws her will in the trash by mistake. The will is burned. The will is not revoked because there was no intent on Mary's part to revoke.*

Example(s): *Example B: Steven executes a valid will leaving his entire estate to Jill. Steven later changes his mind and decides to leave one-half of his estate to Jack. Steven executes another will and includes a provision that specifically revokes the first will. Steven also writes "REVOKED" on the top and across all signatures on the first will, dates it, and signs it. The court will probably honor the revocation of the first will and uphold the validity of the second will.*

What types of wills are there?

Preprinted wills

Preprinted wills or wills generated by computer software packages are legally valid in some states. However, they are generally inappropriate for people with more than small, uncomplicated estates because of their one-size-fits-all nature. Instead, they may be an appropriate starting place for determining what type of property you own and to whom you want to leave it.

Holographic wills

Holographic wills are permitted in some states, but only under certain conditions. A holographic will is a will that is valid despite not being witnessed, because it is written entirely in the testator's handwriting.

Nuncupative wills

Oral or nuncupative wills are recognized by very few states and only in very limited circumstances--usually when a person is near death, has no will, and has no time to write one. Often, states require that the provisions of an oral will be committed to writing soon after they are stated, and they limit the value and type of property that can be distributed in this manner.

Video wills

Currently, no state accepts a videotaped will. However, if you are concerned about challenges to your will, a video showing how the will was executed may help prove that you were of sound mind or that the will was executed properly.

Pourover will

With a pourover will , you can leave all or part of your estate to a trust after your death.

Joint will

A joint will is a single will that serves two or more people. Joint wills are extremely rare and generally undesirable.

Mutual will

A mutual will is drawn up by one individual and is conditioned on an agreement with a second individual to dispose of his or her property in a particular way. It is sometimes called a contractual will. Like joint wills, mutual wills are quite rare and generally undesirable.

Living will

Unlike a traditional will, which disposes of your property, a living will specifies which medical means, if any, are to be used to keep you alive under certain conditions.

Understanding Probate

When you die, you leave behind your estate. Your estate consists of your assets — all of your money, real estate, and worldly belongings. Your estate also includes your debts, expenses, and unpaid taxes. After you die, somebody must take charge of your estate and settle your affairs. This person will take your estate through probate, a court-supervised process that winds up your financial affairs after your death. The proceedings take place in the state where you were living at the time of your death. Owning property in more than one state can result in multiple probate proceedings. This is known as ancillary probate.

How does probate start?

If your estate is subject to probate, someone (usually a family member) begins the process by filing an application for the probate of your will. The application is known as a petition. The petitioner brings it to the probate court along with your will. Usually, the petitioner will file an application for the appointment of an executor at the same time. The court first rules on the validity of the will. Assuming that the will meets all of your state's legal requirements, the court will then rule on the application for an executor. If the executor meets your state's requirements and is otherwise fit to serve, the court generally approves the application.

What's an executor?

The executor is the person whom you choose to handle the settlement of your estate. Typically, the executor is a spouse or a close family member, but you may want to name a professional executor, such as a bank or attorney. You'll want to choose someone whom you trust will be able to carry out your wishes as stated in the will. The executor has a fiduciary duty — that is, a heightened responsibility to be honest, impartial, and financially responsible. Now, this doesn't mean that your executor has to be an attorney or tax wizard, but merely has the common sense to know when to ask for specialized advice.

Your executor's duties may include:

- Finding and collecting your assets, including outstanding debts owed to you
- Inventorying and appraising your assets
- Giving notice to your creditors (e.g., credit card companies, banks, retail stores)
- Filing an estate tax return and paying estate taxes, if any
- Paying any debts or other taxes
- Distributing your assets according to your will and the law
- Providing a detailed report of how the estate was settled to the court and all interested parties

The probate court supervises and oversees the entire process. Some states allow a less formal process if the estate is small and there are no complicated issues to resolve. In those states allowing informal probate, the court may be involved only indirectly. This may speed up the probate process, which can take years.

What if you don't name an executor?

If you don't name an executor in your will, or if the executor can't serve for some reason, the court will appoint an administrator to settle your estate according to the terms of your will. If you die without a will, the court will also appoint an administrator to settle your estate. This administrator will follow a special set of laws, known as intestacy laws, that are made for such situations.

Is all of your property subject to probate?

Although most assets in your estate may pass through the probate process, other assets may not. It often depends on the type of asset or how an asset is titled. For example, many married couples own their residence jointly with rights of survivorship. Property owned in this manner bypasses probate entirely and passes by "operation of law." That is, at death, the property passes directly to the joint owner regardless of the terms of the will and without going through probate. Other assets that may bypass probate include:

- Investments and bank accounts set up to pass automatically to a named person at death (payable on death)
- Life insurance policies with a named beneficiary (someone other than the estate)
- Retirement plans with a named beneficiary
- Other property owned jointly with rights of survivorship

Bypassing Probate

You may have heard about the horrors of probate, but in truth, probate has gotten an undeservedly bad reputation, especially in recent years. If you bypass probate, your estate will go to your beneficiaries without any court proceeding, and you may save a certain amount of time and expenses. However, there is usually little reason for most people to avoid probate today. States continue to revise their probate laws, making them more consumer friendly, particularly for small estates. For most modestly sized estates, the probate process now costs little. In fact, there are some good reasons to distribute your property by will. Decisions are binding and have legal finality once your will is probated. Creditors who fail to file claims against your estate within a specific amount of time — usually six months after receiving notice — are out of luck.

However, some major drawbacks to probate do exist, including the time it can take. The process averages six to nine months to complete but may take up to two years or more for some complex estates, tying up the assets that your family may need immediately. Also, for a larger estate, the cost may be as high as 5 percent of the estate's value.

If you feel that the size and complexity of your estate warrant exploring alternatives to probate, you may want to consider one or more of the following:

Transfer your assets to a revocable living trust

A trust is like a basket that holds your assets. A revocable living trust (also known as an inter vivos trust) is flexible enough to include almost any asset that you own. While you are living, you can act as the trustee and can add or remove property as you see fit. You can also terminate or amend the trust at any time. When you die, your successor trustee distributes the trust assets to the trust beneficiaries, according to the trust agreement. Trusts require a significant amount of paperwork, are costly to create and maintain, and usually require a lawyer to draw up the trust documents. Also, a revocable living trust does not shield your estate from your creditors, creditors of your estate, or estate taxes.

Own property as joint tenancy with rights of survivorship

Assets owned as joint tenancy with rights of survivorship pass automatically to the surviving joint owner(s) at your death. To establish joint ownership, you may need to record new real estate deeds, titles for your car or boat, stock and bond certificates, statements of account for mutual funds, registration cards for your bank accounts, and other assets. This costs little and usually does not require a lawyer. Some drawbacks are that the joint owner has immediate access to your property, and your joint owner's creditors may reach the jointly held property.

Designate beneficiaries

Assets pass outside of probate if you establish payable-on-death provisions for your savings accounts and CDs. Ask your agent to set up transfer-on-death provisions for brokerage accounts containing stocks, bonds, or mutual funds. Your retirement accounts, such as profit-sharing plans, 401(k)s, and IRAs can also pass along to designated beneficiaries. Finally, life insurance death proceeds will avoid probate, provided you name a beneficiary other than your estate.

Make lifetime gifts

Another way to avoid probate is to simply give away your property to your beneficiaries while you are living. Carefully planned gifting can also free those assets from gift and estate taxes. The following are usually nontaxable gifts:

- Gifts to your spouse
- Gifts to qualified charities
- Gifts totaling $15,000 (in 2020) or less per person, per year ($30,000 in 2020 if you and your spouse can split the gifts)
- Tuition payments on behalf of an individual directly to an educational institution
- Medical care expenses paid directly to the provider on behalf of an individual

Other ways to bypass or minimize probate

If your estate is small enough to meet state guidelines, your beneficiaries can simply claim your assets by presenting a notarized affidavit. About half of the states set a limit of $10,000 to $20,000 of the qualified estate value; most of the other states allow as much as $100,000. You can generally deduct estate expenses from your qualified estate value, such as taxes, debts, loans, or family allowance payments, plus the value of any other assets that pass outside probate (e.g., a home jointly owned with a spouse). Real estate is usually disqualified from claims by affidavit. Therefore, your estate may qualify even if it is fairly large. Expect the process to take 30 to 45 days. Another method is for your executor to file for summary, or simplified probate. This streamlined process is generally a paper filing only, requiring no attorney. States vary widely regarding the allowable size of an estate for simplified probate.

Wills: The Cornerstone of Your Estate Plan

If you care about what happens to your money, home, and other property after you die, you need to do some estate planning. There are many tools you can use to achieve your estate planning goals, but a will is probably the most vital. Even if you're young or your estate is modest, you should always have a legally valid and up-to-date will. This is especially important if you have minor children because, in many states, your will is the only legal way you can name a guardian for them. Although a will doesn't have to be drafted by an attorney to be valid, seeking an attorney's help can ensure that your will accomplishes what you intend.

Wills avoid intestacy

Probably the greatest advantage of a will is that it allows you to avoid intestacy. That is, with a will you get to choose who will get your property, rather than leave it up to state law. State intestate succession laws, in effect, provide a will for you if you die without one. This "intestate's will" distributes your property, in general terms, to your closest blood relatives in proportions dictated by law. However, the state's distribution may not be what you would have wanted. Intestacy also has other disadvantages, which include the possibility that your estate will owe more taxes than it would if you had created a valid will.

Wills distribute property according to your wishes

Wills allow you to leave bequests (gifts) to anyone you want. You can leave your property to a surviving spouse, a child, other relatives, friends, a trust, a charity, or anyone you choose. There are some limits, however, on how you can distribute property using a will. For instance, your spouse may have certain rights with respect to your property, regardless of the provisions of your will.

Gifts through your will take the form of specific bequests (e.g., an heirloom, jewelry, furniture, or cash), general bequests (e.g., a percentage of your property), or a residuary bequest of what's left after your other gifts.

Wills allow you to nominate a guardian for your minor children

In many states, a will is your only means of stating who you want to act as legal guardian for your minor children if you die. You can name a personal guardian, who takes personal custody of the children, and a property guardian, who manages the children's assets. This can be the same person or different people. The probate court has final approval, but courts will usually approve your choice of guardian unless there are compelling reasons not to.

Wills allow you to nominate an executor

A will allows you to designate a person as your executor to act as your legal representative after your death. An executor carries out many estate settlement tasks, including locating your will, collecting your assets, paying legitimate creditor claims, paying any taxes owed by your estate, and distributing any remaining assets to your beneficiaries. Like naming a guardian, the probate court has final approval but will usually approve whomever you nominate.

Wills specify how to pay estate taxes and other expenses

The way in which estate taxes and other expenses are divided among your heirs is generally determined by state law unless you direct otherwise in your will. To ensure that the specific bequests you make to your beneficiaries are not reduced by taxes and other expenses, you can provide in your will that these costs be paid from your residuary estate. Or, you can specify which assets should be used or sold to pay these costs.

Wills can create a testamentary trust

You can create a trust in your will, known as a testamentary trust, that comes into being when your will is probated. Your will sets out the terms of the trust, such as who the trustee is, who the beneficiaries are, how the trust is funded, how the distributions should be made, and when the trust terminates. This can be especially important if you have a spouse or minor children who are unable to manage assets or property themselves.

Wills can fund a living trust

A living trust is a trust that you create during your lifetime. If you have a living trust, your will can transfer any assets that were not transferred to the trust while you were alive. This is known as a pourover will because the will "pours over" your estate to your living trust.

Wills can help minimize taxes

Your will gives you the chance to minimize taxes and other costs. For instance, if you draft a will that leaves your entire estate to your U.S. citizen spouse, none of your property will be taxable when you die (if your spouse survives you) because it is fully deductible under the unlimited marital deduction. However, if your estate is distributed according to intestacy rules, a portion of the property may be subject to estate taxes if it is distributed to heirs other than your U.S. citizen spouse.

Assets disposed of through a will are subject to probate

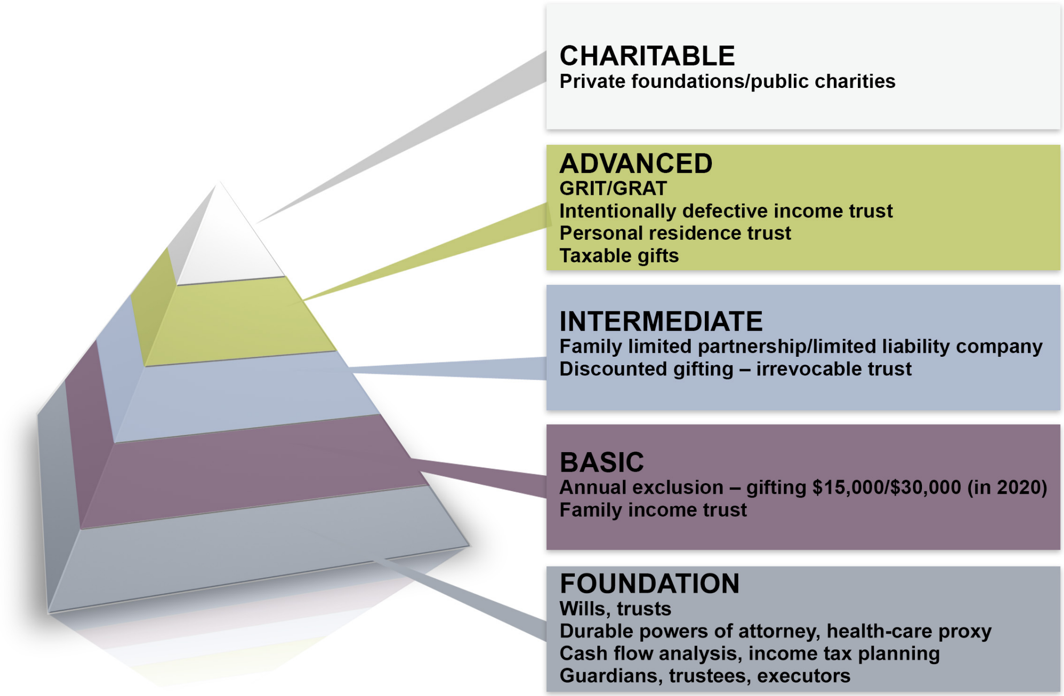
Probate is the court-supervised process of administering and proving a will. Probate can be expensive and time consuming, and probate records are available to the public. Several factors can affect the length of probate, including the size and complexity of the estate, challenges to the will or its provisions, creditor claims against the estate, state probate laws, the state court system, and tax issues. Owning property in more than one state can result in multiple probate proceedings. This is known as ancillary probate. Generally, real estate is probated in the state in which it is located, and personal property is probated in the state in which you are domiciled (i.e., reside) at the time of your death.

Will provisions can be challenged in court

Although it doesn't happen often, the validity of your will can be challenged, usually by an unhappy beneficiary or a disinherited heir. Some common claims include:

- You lacked testamentary capacity when you signed the will
- You were unduly influenced by another individual when you drew up the will
- The will was forged or was otherwise improperly executed
- The will was revoked

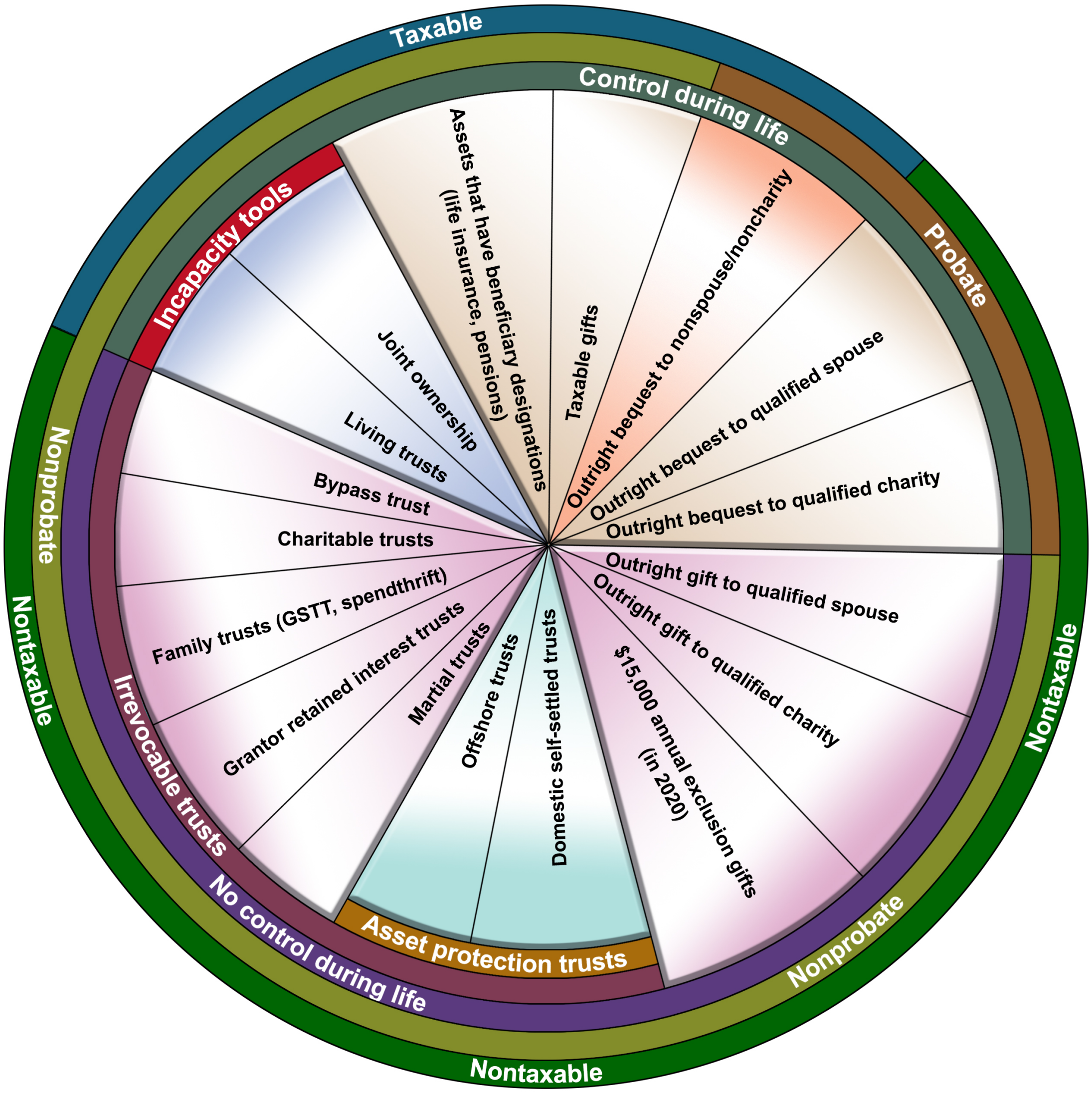
Estate Planning Pyramid



Steps to Estate Planning Success

The World of Estate Planning

A successful estate plan is shaped by goals. Key estate planning goals are minimizing taxes, avoiding probate, retaining control over property, protecting assets, and protecting against incapacity. These goals are represented in the outer rings of the illustration. There are a number of devices that can be employed to accomplish these goals; among them are gifts, wills, trusts (living or irrevocable), joint ownership arrangements, and beneficiary designations. These devices are represented within the world's core (the pie-shaped pieces). This tool has been designed to easily match goals with devices that can achieve those goals.



Selecting an Executor

What is an executor?

An executor is a personal representative who acts for you after your death. You nominate or designate an executor in your will to settle your estate. The person chosen will act in your place to make decisions you would have made if you were still alive. The probate court has final approval, but the court will generally confirm your nomination unless there are compelling reasons not to. An executor's responsibilities typically last from nine months to three years (although, an estate may remain open for several years because of will contests or tax problems). The functions of an executor are varied, but generally your executor:

- Locates and probates your will
- Inventories, collects, and sells (if necessary) your assets
- Pays legitimate creditor claims
- Pays any taxes owed by your estate
- Distributes any remaining assets to your beneficiaries

Tip: *Your executor is entitled to a fee from your estate for services rendered. The fee can be waived (usually, a close family member will waive the fee).*

What are the duties of an executor?

Your executor acts in a fiduciary capacity . This means that he or she must exercise a high degree of care at all times. Additionally, your executor is under court supervision, subject to its control and approval.

Some states require executors to post a bond, which is later paid back to the executor from the estate (though you may be able to waive this requirement through a will provision). In addition, your executor is personally responsible for ensuring that all the proper tax returns are filed and that any estate taxes due are paid. Finally, your executor is accountable to the court and to your beneficiaries on completion of his or her duties.

How do you select an executor?

Your choice of executor is a very important one. Ideally, you want someone you can trust, who has a close relationship to your family, who has some understanding of tax laws, and who has a keen sense of business (especially if you are a business owner).

Typically, spouses are named. Other choices include older children, siblings, or parents. Friends, attorneys, and bank or trust officers are also common. You can name multiple executors to oversee different aspects of your affairs. However, coexecutors may result in an increase in paperwork and a slowdown in the probate process. Some of the attributes you should look for in a good executor are:

- Ability to serve
- Willingness to serve
- Competency
- Trustworthiness
- Appreciation of your family's needs
- Knowledge and experience

Individual versus professional

When choosing an executor, you can name an individual or a professional (e.g., an attorney or a bank trust department) to handle your affairs.

A family member or close friend has knowledge of your affairs and would take a personal interest in the settlement of your estate and the well-being of your beneficiaries. However, he or she may not be the best choice. Serving as an executor is a time consuming and stressful task. Some of the executor's duties are very demanding: preparing and filing tax returns, obtaining appraisals, making an accurate accounting, and these are things best left to professionals. By naming a professional to manage your affairs, you gain some permanence. A professional executor is unlikely to refuse to serve or to resign. In addition, it may be easier to hold a professional executor financially accountable for mismanagement than a nonprofessional. A professional who makes money from managing estates will have the investment expertise as well as the legal, tax, accounting, and computer abilities to do the job well and efficiently. You also gain some impartiality by having a professional manage your affairs. A professional executor should be more impartial to your beneficiaries or heirs. You also reduce the risk that your executor will make hardship loans to friends. However, by nominating a professional, you lose that personal touch from a friend or a relative who is not managing any other estates.

Technical Note: *In general, state laws require that the person who manages your affairs be an adult U.S. citizen. Additionally, your executor cannot be a convicted felon. State laws may also give special powers to your executor, or spell out what your executor can or cannot do. You can also use your will to grant your executor any special powers needed to carry out the instructions in your will.*

What if you don't leave a will?

If you leave no will, if you do not name an executor in your will, or if your executor refuses or fails to serve, the probate court will appoint an administrator (or curator). If this happens, you have no say about who will manage your final affairs. An administrator performs many of the same functions as an executor but has much less power and authority.

Trusts

What is a trust?

A trust is a legal entity that is created when you transfer property to a trustee for the benefit of a third person. The trustee manages the property for the beneficiary in accordance with the terms and the instructions in the trust document. In legal terms, the trustee has legal ownership of the property, while the beneficiary has beneficial ownership.

Creator of trust

The person who creates the trust is called the grantor, settlor, donor, or trustor. The grantor usually decides what assets will be transferred to the trust, who the beneficiaries will be, what the terms and conditions of the trust will be, and who will be the trustee. The grantor may also be a trustee and/or a beneficiary. Moreover, a beneficiary can be a trustee. The only arrangement that will not work is if the sole trustee is also the sole beneficiary (the legal and beneficial interests are said to merge and the trust is therefore disregarded as a legal entity).

Trust document

To create a trust, you usually have to have a written document (called a deed or agreement) that provides the terms of the trust. In most cases, an attorney should draft the trust document. Among other things, the trust document names a trustee, directs the trustee about how to manage and invest the assets in the trust, names the beneficiaries of the trust, and instructs the trustee regarding when to pay out income and principal to the beneficiaries. The trust document may give explicit and detailed instructions about these duties. Alternatively, the trust document may give only very broad and simple guidance. Furthermore, the trust document may give instructions for the distribution of principal which differ from instructions for the distribution of the income generated by the trust. For example, it is very common that a trust document will instruct the trustee to distribute the income to one or more beneficiaries and then pay out the principal to completely different beneficiaries at some point in the future.

Trustee

The grantor selects the trustee. There can be one trustee or multiple trustees. The trustee can be an individual or a corporate trustee (such as a bank trust department). Some trusts may have both a corporate trustee and an individual trustee. The trustee assumes responsibility for the management and distribution of the assets in the trust. The trustee's duties include making numerous complex legal, investment, and fiduciary decisions. Therefore, the selection of trustee should not be taken lightly. There are many factors that should be considered before selecting a trustee, such as the size of the trust, the purpose of the trust, the duration of the trust, the location of beneficiaries, and the tax ramifications.

In certain situations, the grantor can name himself or herself as trustee. A family member can be appointed as trustee, as can a friend, the attorney who drafts the trust, or your accountant. Finally, a corporate trustee, such as a bank trust department or an independent trust company can be named. You should probably discuss all of these options with an attorney.

Location of trust

In addition to choosing a trustee, you must also decide where the trust will be located. You have the option of setting up a trust in any state. State law governs how a trust is created and maintained, and these laws vary dramatically from state to state. There are also variations in state gift, estate, and income tax laws, as well as differences from state to state in the rights and obligations of the trustee and the beneficiaries. For example, some states provide better creditor protection to trusts than other states. Therefore, the decision regarding where to set up your trust should be discussed with your attorney.

Trust assets

Another decision you will face in setting up a trust is: Which assets should you transfer to the trust? The type of asset that you may transfer to a trust is almost limitless. You can transfer cash, stocks, bonds, insurance policies, real estate, your personal residence, artwork, and almost any other type of asset. The type of asset that you might transfer to a trust depends on what assets you currently own and what your goals are. For example, if you want to provide the beneficiaries with income, you may want to transfer bonds or high-yield stocks. If your goal is to provide the beneficiaries with liquidity to pay estate taxes, you may want to transfer a life insurance policy.

Types of trusts

There are several different types of trusts that you can create. You can create a trust in your will (this is called a testamentary trust), or you can create a trust during your life (this is called a living trust). You can create a revocable trust (this kind of trust you can amend or revoke), or an irrevocable trust (this kind of trust you cannot amend or revoke).

Testamentary trust

A testamentary trust is one that is created and funded under the terms of your will. It does not come into existence until your death. Assets that are transferred to the trust must pass through probate.

Until your death, you can change the terms of the trust by amending your will. Upon your death, the trust becomes irrevocable.

A testamentary trust can be contingent. That means that it will be created upon your death only if certain conditions are present (e.g., your children are under a certain age).

Living trust

A living trust, also called an inter vivos trust, is created while you are living. A living trust can either end or continue at your death. Property in the trust is distributed according to the terms of the trust, not your will. Living trust assets avoid probate.

Revocable trust

As the name implies, you can revoke or amend the terms of a revocable trust. You can change the beneficiaries or trustee. You can add or remove assets from the trust. You can also change the provisions of the trust. You can even dissolve the trust. Furthermore, at your death, the assets in the revocable trust do not pass by the terms your will (and thus do not pass through probate). Instead, the assets in a revocable trust are distributed in accordance with the terms of the trust. In fact, many people set up a revocable living trust simply to avoid the delay and cost of probate. However, one big disadvantage to a revocable trust is that the assets in trust will be included in your gross estate for estate tax purposes. Thus, a revocable trust is not used to avoid estate taxes.

Caution: *A revocable trust may become an irrevocable trust at the death of the grantor, unless the grantor gives someone else the power to amend the trust. The spouse of the decedent, for example, cannot change the terms of the trust unless he or she is given a special power of appointment.*

Irrevocable trust

Again, as the name implies, an irrevocable trust is one that you cannot revoke or amend once the trust has been established. This means that you cannot dissolve the trust, change the beneficiaries, remove assets from the trust, or change the terms of the trust. The main advantage to setting up an irrevocable trust is that the assets in the trust, including any future appreciation, are not typically included in your gross estate for estate tax purposes. Of course, the transfer to an irrevocable trust may be a taxable gift , and gift taxes may have to be paid at the time of the transfer. A secondary benefit of an irrevocable trust may be that the assets in the trust are beyond the reach of your creditors.

Irrevocable trusts are used primarily as estate planning tools. With careful planning, you may be able to save substantial amounts in estate taxes. There are many different types of irrevocable trusts that can be set up. To name a few, there is an irrevocable life insurance trust (to hold an insurance policy), a qualified personal residence trust (to hold a personal residence), and a grantor retained annuity trust (to provide you with income).

Why use a trust?

There are many different reasons why you may want to use a trust. For example, you may want to: (1) avoid probate, (2) have professional management of your assets, (3) provide for your minor children, (4) avoid estate taxes, and (5) protect your assets from creditors.

Avoid probate

As noted, assets in both a revocable and irrevocable trust do not pass through probate at your death. The assets are distributed in accordance with the terms of the trust, which may even continue past your death. Your estate, therefore, avoids the cost and delay of probate. A further benefit of using a trust is that you will have increased privacy. A will is a public document (i.e., anyone can go down the probate court and review the contents of your will). However, a trust remains private.

Protect against old age and disability

Another reason to use a trust is to protect yourself in case of a mental or physical disability or other age-related problems. You can set up a trust, name yourself as the beneficiary, and then name yourself and another person as the trustees. If you become infirm or mentally incapacitated, the other trustee can manage your assets for you and distribute those assets in a way that is in your best interest.

Provide for your minor children

You may want to use a trust if you plan to leave your assets to minor children (generally, under age 18). Because you cannot predict when you might die, you may want to set up a contingent trust in your will in case you die when your children are still minors. The assets could then be transferred to the trust, and the trustee could manage the assets and make the necessary distributions when your children reach an older age.

Avoid estate taxes

Assets that have been transferred to an irrevocable trust are typically not included in your gross estate for estate tax purposes. (This result assumes that the creator of the trust is not a beneficiary of the trust. Furthermore, if the creator is also the trustee, then his or her ability to make distributions to the beneficiaries must be limited to ascertainable standards.) It is important to note, however, that gift taxes may have to be paid at the time of the original transfer to the trust. However, any appreciation in the assets after the transfer should avoid both estate and gift taxes.

Caution: *One exception to the general rule that assets transferred to an irrevocable trust are not included your gross estate is a life insurance policy. If you transfer a life insurance policy to an irrevocable trust within three years of your death, then the insurance policy will be pulled back into your gross estate.*

Reduce income taxes

By transferring income-producing assets to certain types of trusts, you may be able to transfer income to those heirs who are in a lower income tax bracket than you. By doing this, you may be able to reduce your own income taxes.

Benefit a charity

There are certain types of trusts where you transfer assets to the trust, receive income from the trust for a period of time, and then leave the assets to a charity upon your death. These types of trusts may provide you with both income and estate tax benefits, and also allow you to give to your favorite charity.

Other benefits

There are numerous other reasons why you may want to transfer your assets using a trust. These other benefits are beyond the scope of this general discussion. Please consult an estate planning attorney or other resources.

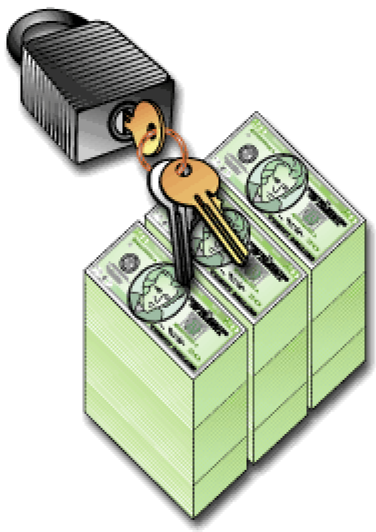
Advantages of Trusts

Why you might consider discussing trusts with your attorney

- Trusts may be used to minimize estate taxes for married individuals with substantial assets.
- Trusts provide management assistance for your heirs.*
- Contingent trusts for minors (which take effect in the event that both parents die) may be used to avoid the costs of having a court-appointed guardian to manage your children's assets.
- Properly funded trusts avoid many of the administrative costs of probate (e.g., attorney fees, document filing fees).
- Generally, revocable living trusts will keep the distribution of your estate private.
- Trusts can be used to dispense income to intermediate beneficiaries (e.g., children, elderly parents) before final property distribution.
- Trusts can ensure that assets go to your intended beneficiaries. For example, if you have children from a prior marriage you can make sure that they, as well as a current spouse, are provided for.
- Trusts can minimize income taxes by allowing the shifting of income among beneficiaries.
- Properly structured irrevocable life insurance trusts can provide liquidity for estate settlement needs while removing the policy proceeds from estate taxation at the death of the insured.

What is a trust?

A trust is a legal entity that is created for the purpose of transferring property to a trustee for the benefit of a third person (beneficiary). The trustee manages the property for the beneficiary according to the terms specified in the trust document.



*This is particularly important for minors and incapacitated adults who may need support, maintenance, and/or education over a long period of time, or for adults who have difficulty managing money.

Minimizing Estate Taxes

What is minimizing estate taxes?

The act of giving away your property, either during life or at death, will probably be subject to one or more of several types of taxes (collectively referred to here as estate taxes), either on the federal level, state level, or both. These tax liabilities may be the largest potential expenses you or your estate may have to pay; federal estate tax alone may reach as high as 40 percent of your estate if you die in 2020. This also means that property you intend to go to your loved ones or others when you die may go instead to the IRS or to your state. Therefore, understanding how these taxes can be minimized is vital if you want to preserve your estate for others.

What are estate taxes?

Estate taxes are actually transfer taxes. Transfer taxes are imposed when you give your property to someone else. This can be done during life (this kind of transfer is called a gift) or at death (this kind of transfer is called a bequest or legacy if you leave a will, and intestate succession if you don't leave a will). There are five transfer taxes that may affect your estate: (1) state gift tax, (2) state death taxes, (3) state generation-skipping transfer (GST) tax, (4) the federal gift and estate tax, and (5) the federal GST tax.

State gift tax

Currently, only a few states impose a gift tax. A gift is a transfer of property you (the donor) make during your lifetime. The person or organization you give to is called the donee. When you make a gift, it is in exchange for nothing or in exchange for property of lesser value (in other words, it is not a bona fide sale). Generally, gifts must be reported, and gift tax paid in the year following the year in which the gift is made (e.g., gift tax on a gift made in 2019 would be due in 2020). If your state imposes a gift tax and you intend to make lifetime gifts, you should contact your state's department of revenue to find out what gifts need to be reported, how to compute the gift tax, and when and how to file a gift tax return.

State death taxes

State death taxes are imposed on property distributed after your death. You should be especially aware of state death taxes because they may affect even the smallest estates. There are three types of state death taxes: inheritance tax, estate tax, and credit estate tax (commonly referred to as a sponge tax or pickup tax). Many states impose at least one type.

State generation-skipping transfer (GST) tax

Currently, some states impose a GST tax. The GST tax is imposed on property transferred to a family member who is two or more generations below you (e.g., a grandchild or great-nephew). You can contact your state's department of revenue to find out what transfers may be subject to state GST tax, and when and how to file a return.

Federal gift and estate tax

Generally speaking, the federal gift and estate tax is imposed on property transferred to others either while you are living or at the time of your death. Unlike the individual states which generally impose at least one type of death tax, and some of which impose a separate gift tax, the federal tax system is unified. In other words, the IRS adds lifetime transfers and transfers made at death and treats them the same. This is how the unified tax system works:

Before 1976, the federal tax system worked much like that of the states. Gifts made during life (taxable gifts) were reported, and any gift tax owed was paid on an annual basis. After death, estate tax was imposed only on property owned at death (gross taxable estate). Since 1976, generally, taxable gifts are still reported, and any gift tax owed is paid annually (generally, you must file a gift tax return and pay gift tax due, if any, by April 15 of the year following the year in which you make a taxable gift). But upon death, all taxable gifts are added to your gross taxable estate for estate tax calculation purposes, even though a gift tax return may already be filed and gift tax paid (gift tax paid is deducted from the estate tax owed). The IRS unified the gift tax and estate tax systems so that: (1) you can't avoid estate tax by giving your wealth away before you die, and (2) you pay tax on the cumulative amount of wealth you give away (this pushes your estate into a higher tax bracket).

The federal generation-skipping transfer (GST) tax

Like the state-imposed GST tax, the federal GST tax is a tax imposed on property you transfer to a family member who is two or more generations below you (e.g., a grandchild or great-nephew). The IRS wants to levy a tax on property as it is passed from generation to generation at each and every level. The purpose of the GST tax is to keep families from avoiding estate tax by skipping an intermediate generation. A flat tax rate equal to the highest estate tax rate is imposed on every generation-skipping transfer you make over a certain lifetime amount.

Tip: *The GST tax rate is the same as the maximum estate tax rate, and the GST tax exemption is the same amount as the estate* *tax applicable exclusion amount.*

How do you minimize estate taxes?

You can minimize estate taxes by: (1) taking advantage of certain allowable tax exclusions, deductions, and credits, (2) using an estate freeze technique, or (3) employing post-mortem planning.

Exclusions, deductions, and credits

Under the federal tax system, individuals are generally allowed to make gifts of up to $15,000 (in 2019 and 2020) per donee each year gift tax free under the annual gift tax exclusion.

In addition, individuals are allowed to exempt a certain amount of property from the gift and estate tax.

Further, transfers of property between U.S. citizen spouses are fully deductible, as are transfers of property to qualified charitable organizations.

There are many exclusions, deductions, and credits that if effectively used can minimize estate taxes. You need to understand what these exclusions, deductions, and credits are, and how they work in order to take full advantage of them.

Tip: *States also have their own exclusions, deductions, and credits, although they may not be the same as the federal system.*

Estate freeze

An estate freeze is any planning device that allows you to freeze the present value of your estate and shift any future growth (or potential growth) to your successors.

Example(s): *You give land valued at $100,000 to your children. Twenty-five years later, you die. The land is valued at $500,000 on the date of your death, but only $100,000 is included in your taxable estate because the value of the land froze on the date you gave it to your children.*

There are many ways you can freeze the value of property. Estate freezing techniques range from relatively simple (e.g., installment sale or private annuity) to the more complex (e.g., gift- or sale-leaseback). You need to know what these techniques are and how they are used in order to know which, if any, is best for you.

Tip: *This generally works for state taxes also.*

Post-mortem planning

There are many post-mortem (i.e., "after death") techniques that can help keep the value of your property as low as possible in order to minimize federal estate taxes. There are a number of post-mortem techniques that you should know about. Even though these techniques are implemented after your death, you should understand each of them now because if you believe your estate might benefit from them, there may be things you need to do now to ensure that your estate will qualify for these elections after your death.

Common Incapacity Documents

Durable Power of Attorney for Health Care (DPAHC)/Health-Care Proxy	
Advantages	**Disadvantages**
• Is flexible--allows your representative to act on your behalf and make medical decisions based on current circumstances • Generally, your representative can make any decision you would be allowed to make • Generally can be used any time you become incompetent	• Not practical in an emergency--your representative must be present to act on your behalf • Not permitted in some states
Living Will	
Advantages	**Disadvantages**
• Allows you to convey decisions regarding your medical care without relying on any one person to carry out your wishes	• Generally can be used only if you are terminally ill or injured, or in a persistent vegetative state • Generally used only to make decisions regarding life-sustaining treatments • Emergency medical personnel generally cannot withhold emergency care based on a living will • Not permitted in some states
Do Not Resuscitate (DNR) Order	
Advantages	**Disadvantages**
• Allows you to decline CPR if your heart or breathing fails • Effective in an emergency--your doctor should note an in-hospital DNR order on your chart. Out-of-hospital DNR orders take various forms, depending on the laws of your state. ID bracelets, MedicAlert ®necklaces, and wallet cards are some methods of noting DNR status.	• Some states allow DNR orders only for hospitalized patients--others do not restrict eligibility • Only used to decline CPR in case of cardiac or respiratory arrest • Not permitted in some states
Durable Power of Attorney (DPOA)	
Advantages	**Disadvantages**
• You control who acts and what they can do with your property • Low cost to implement • Decreases the chance of court intervention	• Some states do not permit a "springing" DPOA (i.e., a DPOA that is effective only after you have become incapacitated)

Estate Planning Checklist

General information	Yes	No	N/A
1. Has relevant personal information been gathered? • Personal details • Family details • Current advisory team • Goals and expectations	❑	❑	❑
2. Has financial situation been assessed? • Assets • Liabilities • Life insurance policies • Other insurance coverage • Income • Expenses	❑	❑	❑
3. Have current documents been reviewed? • Will • Trust documents • Power of attorneys • Medical directives • Insurance policies • Buy-sell agreements • Deeds, leases, mortgages, and land contracts • Guardian nominations • Separation/divorce agreements • Tax returns	❑	❑	❑
4. Have funeral arrangements been made?	❑	❑	❑
Notes:			

Basics	Yes	No	N/A
1. Is there currently a valid will?	❑	❑	❑
2. If yes, does will reflect current goals and objectives?	❑	❑	❑
3. Does choice of executor remain appropriate?	❑	❑	❑
4. Has durable power of attorney been executed?	❑	❑	❑
5. Have medical directives been executed?	❑	❑	❑
6. Have beneficiary designations for retirement plans and life insurance policies been reviewed?	❑	❑	❑
7. Has impact of probate been considered?	❑	❑	❑

Notes:			

Trusts	Yes	No	N/A
1. Is the use of a living trust appropriate?	❑	❑	❑
2. Is the use of a testamentary trust appropriate?	❑	❑	❑
3. Is the use of an irrevocable life insurance trust appropriate?	❑	❑	❑
4. Do existing trusts, if any, continue to meet overall objectives?	❑	❑	❑
Notes:			

Estate tax	Yes	No	N/A
1. Has estate plan been reviewed due to changing tax laws?	❑	❑	❑
2. Has impact of estate tax been evaluated?	❑	❑	❑
3. Have options to minimize estate tax been explored? • Lifetime gifting • Full use of basic (applicable) exclusion amount and marital deduction • Qualified terminable interest property (QTIP) elections • Qualified domestic trust (QDT) for noncitizen spouse • Charitable giving • Grantor retained trusts • Family limited partnership (FLP)/limited liability company (LLC)	❑	❑	❑
Notes:			

Lifetime gifting	Yes	No	N/A
1. Have gifts been made?	❑	❑	❑
2. Has a lifetime gifting strategy been implemented?	❑	❑	❑
3. Are gift tax consequences understood?	❑	❑	❑
4. Has consideration been given to types of property suitable for gifting?	❑	❑	❑

5. Is valuation discount planning understood?	❑	❑	❑
Notes:			
Charitable intentions	**Yes**	**No**	**N/A**
1. Have charitable gifts or bequests been planned?	❑	❑	❑
2. Is a charitable trust appropriate? • Charitable lead trust • Charitable remainder trust • Pooled income fund • Private foundation • Donor-advised fund	❑	❑	❑
3. Is a charitable gift annuity appropriate?	❑	❑	❑
4. Is the charitable gift of a remainder interest in a home or farm appropriate?	❑	❑	❑
Notes:			
Life insurance issues	**Yes**	**No**	**N/A**
1. Have liquidity needs of estate at death been evaluated?	❑	❑	❑
2. Is current life insurance coverage appropriate?	❑	❑	❑
3. Have steps been taken to keep life insurance proceeds out of taxable estate? • Policy ownership • Irrevocable life insurance trust	❑	❑	❑
4. Have beneficiary choices been evaluated in light of overall estate plan?	❑	❑	❑
Notes:			
Business interests	**Yes**	**No**	**N/A**

1. Have provisions been made to transfer business interest? • Buy-sell agreement and necessary funding • Sell business • Transfer business with lifetime gifts • Key person buyout	❑	❑	❑
2. Is liquidation an option?	❑	❑	❑
Notes:			

Conducting a Periodic Review of Your Estate Plan

What is conducting a periodic review of your estate plan?

With your estate plan successfully implemented, one final but critical step remains: carrying out a periodic review and update.

Imagine this: since you implemented your estate plan five years ago, you got divorced and remarried, sold your house and bought a boat to live on, sold your legal practice and invested the money that provides you with enough income so you no longer have to work, and reconciled with your estranged daughter. This scenario may look more like fantasy than reality, but imagine how these major changes over a five-year period may affect your estate. And that's without considering changes in tax laws, the stock market, the economic climate, or other external factors. After all, if the only constant is change, it isn't unreasonable to speculate that your wishes have changed, the advantages you sought have eroded or vanished, or even that new opportunities now exist that could offer a better value for your estate. A periodic review can give you peace of mind.

When should you conduct a review of your estate plan?

Every year for large estates

Those of you with large estates (over the applicable exclusion amount) should review your plan annually or at certain life events that are suggested in the following paragraphs. Not a year goes by without significant changes in the tax laws. You need to stay on top of these to get the best results.

Every five years for small estates

Those of you with smaller estates (under the applicable exclusion amount) need only review every five years or following changes in your life events. Your estate will not be as affected by economic factors and changes in the tax laws as a larger estate might be. However, your personal situation is bound to change, and reviewing every five years will bring your plan up to date with your current situation.

Upon changes in estate valuation

If the value of your estate has changed more than 20 percent over the last two years, you may need to update your estate plan.

Upon economic changes

You need to review your estate plan if there has been a change in the value of your assets or your income level or requirements, or if you are retiring.

Upon changes in occupation or employment

If you or your spouse changed jobs, you may need to make revisions in your estate plan.

Upon changes in family situations

You need to update your plan if: (1) your (or your children's or grandchildren's) marital status has changed, (2) a child (or grandchild) has been born or adopted, (3) your spouse, child, or grandchild has died, (4) you or a close family member has become ill or incapacitated, or (5) other individuals (e.g., your parents) have become dependent on you. For example, many states have a law revoking all or part of your will if you divorce or remarry.

Upon changes in your closely held business interest

A review is in order if you have: (1) formed, purchased, or sold a closely held business, (2) reorganized or liquidated a closely held business, (3) instituted a pension plan, (4) executed a buy-sell agreement, (5) deferred compensation, or (6) changed employee benefits.

Upon changes in the estate plan

Of course, if you make a change in part of your estate plan (e.g., create a trust, execute a codicil, etc.), you should review the estate plan as a whole to ensure that it remains cohesive and effective.

Upon major transactions

Be sure to check your plan if you have: (1) received a sizable inheritance, bequest, or similar disposition, (2) made or received substantial gifts, (3) borrowed or lent substantial amounts of money, (4) purchased, leased, or sold material assets or investments, (5) changed residences, (6) changed significant property ownership, or (7) become involved in a lawsuit.

Upon changes in insurance coverage

Making changes in your insurance coverage may change your estate planning needs or may make changes necessary. Therefore, inform your estate planning advisor if you make any change to life insurance, health insurance, disability insurance, medical insurance, liability insurance, or beneficiary designations.

Upon death of trustee/executor/guardian

If a designated trustee, executor, or guardian dies or changes his or her mind about serving, you need to revise the parts of your estate plan affected (e.g., the trust agreement and your will) to replace that individual.

Upon other important changes

None of us has a crystal ball. We can't think of all the conditions that should prompt us to review and revise our estate plans. Use your common sense. Have your feelings about charity changed? Has your son finally become financially responsible? Has your spouse's health been declining? Are your children through college now? All you need to do is give it a little thought from time to time.

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