

# The Basics of Estate Planning

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# Two Different Phases of Estate Planning

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- Planning in the event of your incapacity (you are still living)
- Planning for your death

# Documents Commonly Used In Planning for Incapacity

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- Financial/Durable Power of Attorney
- Health Care Power of Attorney
- Living Will

# Financial Powers of Attorney

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- Authorizes another to act on your behalf with regard to property
- Effective immediately vs. effective upon incapacity
- Required to be recorded with Register of Deeds before transferring real estate or in event of incapacity
- Should appoint successors
- Needs to be coordinated with other estate planning documents
- General Power of Attorney vs. Limited Power of Attorney

# Health Care Power of Attorney

- Allows you to appoint another person to make health care decisions for you if you are incapacitated
- Grants broad decision making capabilities, including life support, burial and anatomical gift decisions
- HIPAA release should be in a separate document
- Effective only if principal is unable to make decisions
- NC requires two unrelated witnesses and notary

# Living Will

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- Expresses your wishes regarding the withholding of artificial means of life support and artificial food and hydration
- Statutory form in North Carolina

# Estate Planning in the Event of Death

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# Four Ways to Pass on Property

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- Beneficiary Designation
- Joint Ownership With Right of Survivorship
- Probate
- Trust

# Beneficiary Designations

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- IRAs, 401(k)s, life insurance policies, annuities, transfer on death accounts etc.
- Non-Probate Asset unless Estate is beneficiary
- Takes precedence over Last Will and Testament and Trust
- Review every three years at a minimum to ensure consistency with overall estate plan and to avoid unnecessary income taxes for beneficiaries

# Types of Joint Ownership

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- Right of Survivorship vs. Tenants in Common
- Real property owned by Husband and Wife as Tenants by the Entirety has right of survivorship

# Joint Ownership with Right of Survivorship

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- Non-Probate asset at death of first joint owner
- Takes precedence over Last Will and Testament or Trust
- Beware of unintentional disinheritance
- May expose asset to creditors of the other joint owner (except for tenants by the entirety property)
- Can trigger gift tax if add non-spouse joint owner

# Probate

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- Probate: refers to court supervised process of managing and/or distributing assets of a minor, incompetent or deceased person
- Public Process
- Requires payment of court fees and frequently attorney fees at hourly rates
- NC court fees are \$4 per \$1,000 of probate assets up to a maximum fee of \$6,000
- If a person owns probate assets at death, probate is required with or without a Will

# Testate vs. Intestate

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- Testate: when a person dies with a valid Last Will and Testament
  - Terms of Last Will and Testament control distribution of probate assets
- Intestate: when a person dies without a valid Last Will and Testament
  - Intestacy laws of state of domicile control distribution of probate assets

# Last Will and Testament

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- Name recipients of property
- Name guardian for minor children
- Name Executor of estate
- Unless a trust is created for minors, property passes to beneficiaries at age 18
- Does not come into effect until death of testator

# Reasons to review a Will

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- Change in family circumstances
- Death of a spouse or child
- Divorce
- Birth of new child or grandchild
- Marriage
- Move to different state
- Changes in property

# Reasons to review Will (cont.)

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- Substantial increase or decrease in assets
- Sale or purchase of a business
- Tax law changes

# What is a trust?

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- Written set of instructions directing management of property for the benefit of someone or something

# Trust Terminology

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- Grantor/Settlor: person who establishes trust
- Trustee: person or entity who manages trust property
- Beneficiary: person or entity for whom trust property is being managed
- Corpus/Principal: property owned by the trust

# Different Types of Trusts

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- Revocable Trust vs. Irrevocable Trust
- Living Trust vs. Testamentary Trust

# Revocable Living Trusts

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- Used to avoid Probate at death and during lifetime.
- Privacy
- Grantor re-titles assets into the name of the Revocable Trust during lifetime
- Grantor is commonly the beneficiary and Trustee of the trust during lifetime
- Assets owned by the Trust at the time of the Grantor's death pass outside of the probate process

# Trusts Also Used To Control Inheritance

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- Revocable, Irrevocable, Living or Testamentary
- Trust allows Grantor to control distributions beyond the age of 18-Age of Majority in NC
- Can distribute income or principal over a term of years or the lifetime of a Beneficiary
- Beneficiary can still receive distributions for education, health care, support etc. with approval of Trustee

# Specialized Trust Provisions

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- Dollar distributed for a dollar earned
- Achievement distributions/rewards
- Drug and alcohol testing
- Supplemental Needs of a disabled beneficiary to avoid disqualification of benefits
- Generation Skipping Trusts

# Asset Protection Basics

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- Ownership of Property
  - Tenancy by the Entirety
  - Ownership by non-working spouse
  - Marital/Separate Property

# Asset Protection Basics (cont.)

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- Other Techniques
  - Life Insurance
  - Family Limited Partnerships
  - Qualified Retirement Accounts and IRAs
  - Limited Liability Companies
  - Offshore Trusts

# Estate Taxes

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- Estate Taxes are separate from income taxes
- Estate Taxes are assessed on assets in excess of exemption amount
- Your estate includes everything you own or control at time of death including life insurance

# Estate Taxes (cont.)

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- Currently no Federal or North Carolina estate tax (as of 1/1/2010)
- In 2011, Federal and North Carolina estate tax will be reinstated (if not sooner)
- In absence of new legislation in 2010, exemption will default to \$1.0 million in 2011

# Estate Tax

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- Trusts can be established to minimize estate taxes
- Husband and Wife can create trusts that will enable them to combine their exemptions and pass \$2,000,000 to their beneficiaries (or more if higher exemption created by future legislation)

# The "I Love You" Will

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- There is an unlimited Marital Deduction for property passing to a surviving spouse

- Example:

Bill and Mary:

Combined Taxable Estate: \$2 Million

Estate Taxes Due Upon Bill's Death: \$0

# "I Love You" Will continued...

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Upon Mary's Subsequent Death:

Mary's Taxable Estate:	\$2,000,000
Mary's Estate Tax Exemption:	<u>-\$1,000,000</u>
Net Taxable Estate	\$1,000,000
Total Estate Tax Due	\$435,000

# Credit Shelter Trusts

**Bill and Mary**  
**Total Estate = \$2 Million**

Bill Dies First

Mary Dies Second

**Bill's Trust**  
For the benefit of Mary (and issue) during Mary's lifetime

\$1,000,000 Bill's Estate  
-\$1,000,000 Exemption

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\$0 Taxable Estate

**Mary's Trust**  
Property passes at Mary's death to beneficiaries or held in trust for the benefit of named beneficiaries

\$1,000,000 Mary's Estate  
-\$1,000,000 Exemption

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\$0 Taxable Estate

# Irrevocable Trusts

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- May be used to remove assets from a person's estate for estate tax, Medicaid or asset protection purposes
- May involve giving up control and use of assets to achieve the objectives described above
- May have to file separate income tax return
- Used commonly with Life Insurance policies to remove death benefit from the Decedent's estate

# Gift Tax

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- No federal gift tax on transfers between husband and wife (different rules apply for non-citizen spouses) and gifts to charity
- Can make tax-free gifts of up to \$13,000 per year to an unlimited number of beneficiaries
- Medical and educational expenses paid directly to the provider are also gift tax free
- For gifts in excess of those discussed above, there is a Federal lifetime gift tax exemption of \$1,000,000
- North Carolina gift tax repealed 1/1/ 2009

# Charitable Gifts

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- Unlimited charitable gift tax deduction on lifetime gifts to 501(c)(3) organizations.
- Unlimited charitable estate tax deduction for charitable gifts at death.
- Income Tax deduction for lifetime gifts.
- Outright gifts vs. split interest charitable gifts.
- Charitable Gift Annuities and Charitable Remainder Trusts are examples of split interest charitable gifts.

# Charitable Gift Annuities

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- Asset will be transferred to charity in exchange for annuity payments.
- No capital gains upon sale of assets by charity. This also alleviates lack of diversification risk for Donor.
- Income Tax deduction for Donor based on value of gift minus Donor's retained annuity interest.
- Potential increase in income for Donor.

# Charitable Gift Annuities cont.

- **EXAMPLE:** \$1,000,000 of Exxon Stock: Cost Basis \$100,000; yields \$16,000 of annual income.
- Post CGA Income – \$71,000 (7.1% charitable gift annuity payout)
- Income Tax Charitable Deduction – \$415,470 (donor age 75)
- Capital gains tax savings on sale of stock
  - \$900,000 LT Cap Gain avoided (or deferred)
  - \$135,000 Fed Cap Gains tax savings (plus applicable state taxes)
- Reduced portfolio concentration

# Charitable Remainder Trusts

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- Similar to a Charitable Gift Annuity except assets transferred to a Trust rather than directly to a charity.
- Trust pays Donor either an Annuity or a Unitrust amount each year.
- Trust term can be based on the the life of the Donor or the lives of others chosen by Donor, or can be a term of years.

# Charitable Remainder Trust (continued)

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- At the end of the trust term, balance passes to charity.
- Donor can reserve the right to change the charitable remainder beneficiaries during the term of the CRT.

# Charitable Remainder Trust (continued)

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- No capital gains upon sale of assets by Trustee.
- Donor gets an income tax deduction based on present value of the charitable remainder interest.
- Donor's income may increase as a result of the CRT.

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