Arlington LAW GROUP

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Estate Planning Strategies

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What is Estate Planning?

- Estate Planning provides peace of mind **after your death**:
  - A well drafted Will or Trust can save your beneficiaries time, money, and stress.
  - Proper planning can reduce or eliminate estate and death taxes.
  - By combining planning with insurance you can provide for your family and control how they will benefit from your estate.

What is Estate Planning?

- Estate Planning **improves your quality of life** and helps your friends and family care for you:
  - Medical and financial powers of attorney allow your family and friends to make decisions on your behalf and handle your finances if you become disabled or incapacitated during your life.
  - Asset protection trusts ensure that your nest egg is protected, that you receive maximum government benefits, and that you receive the highest standard of care during your life.

Asset Protection and Estate Planning

Legal documents that every adult needs:
- Last Will and Testament
- Durable Financial Power of Attorney
- Advance Medical Directive/Living Will
- Medical Power of Attorney

Taxes, Trusts, and Asset Protection:
- Gift and Estate Taxes for 2016 and beyond
- Revocable (“Living”) Trusts
- Irrevocable Asset Protection Trusts
- Life Insurance Trusts
- Retirement Accounts and Roth IRA Conversions

Probate

- Probate is the court supervised process of collecting the assets of someone who has died, paying debts & distributing to heirs.
- Estates with and without Wills go through Probate.
- Trusts allow assets to pass outside of probate, avoiding the time and expense.
- Only Probate assets are affected.

Probate

- What assets are **not** included in Probate?
  - Jointly titled property with right of survivorship (e.g. house, bank accounts, etc.)
    - Joint Tenants with Right of Survivorship
    - Tenancy by the Entirety (Husband & Wife)
  - Pay-on-death property (e.g. some bank accounts)
  - Designated Beneficiary property (e.g. retirement plans, life insurance, etc.)

Probate

- What assets are included in Probate?
  - Jointly titled property **without** right of survivorship
    - Tenants in Common
    - Heirs Property
  - Accounts in your name only with no designated beneficiaries or pay-on-death provision (e.g. personal checking account).
  - Probate is a bigger issue after the death of the second spouse, or if both spouses die at the same time, when jointly titling assets is insufficient to avoid Probate.

Without a Will: Intestacy

- Without a Will, the state Intestacy laws supply default rules for who will inherit.
- Heirs and order of inheritance are defined by law in each state.
- Virginia Code §64.2-200 and §64.2-201
  - Spouse and children take first.
  - Parents take next if no spouse or children.
  - Siblings take next if no spouse, children or parents.
  - Then on to grandparents, aunts, uncles, cousins, etc.

Without a Will: Intestacy

- Intestacy provides no provisions for:
  - Who becomes guardian of minor children. A court will decide that based upon what it determines is in the best interest of the children.
  - Trusts for minor or special needs children.
  - Specific gifts to individuals or charities.
  - No waiver of bond for executors/administrators.
- Intestate estate goes through probate, and the court appoints an Administrator.

Last Will and Testament

- Commonly referred to as a "Will".
- Covers disposition of all Probate assets.
- Provides directions for guardianship of minor children.
- Designates an Executor to manage the estate.
- May include provisions such as a Testamentary Trust for minor children or children with special needs.

Last Will and Testament

- Providing for your children in your Will:
  - Will allows you to designate guardian(s) for minor children.
  - Will for parents with minor children should contain provisions for the management of money for minor children.
    - Testamentary Trust
    - Uniform Gifts to Minors Act (UGMA) Accounts
    - Uniform Transfers to Minors Act (UTMA) Accounts
    - College Savings Plans (529 Plans)

Last Will and Testament

- Selecting an Executor:
  - Executor of an estate is responsible for making reports to the court, handling finances, paying taxes, etc. This should be someone with good money sense who you trust to handle your affairs. Usually it is your surviving spouse, or if your spouse does not survive you, another trusted person or attorney.
  - Executor may be required to post a bond, or this may be waived.

Last Will and Testament

- Selecting Trustees:
  - If the Will includes a Testamentary Trust for minor children or children with special needs, you will need to select a Trustee.
  - Trustee can be, *but does not have to be*, the same person who will be the guardian for the children.
  - In addition to an individual, you can select an attorney or a financial intuition to act as the trustee, but they will take a fee for managing the trust assets.

Last Will and Testament

- Other Bequests:
  - Your Will may contain specific gifts of money to individuals or organizations.
  - Since your Will only covers your Probate assets, the first spouse to die may have limited funds from which the Will can make gifts.
- Gifts of Tangible Personal Property:
  - Virginia allows for a separate writing for gifts of tangible personal property.
  - This writing may be updated from time to time without going through the full Will execution process.

Last Will and Testament

- Charitable Gifts:
  - Writing a Will or Trust allows you to give gifts to church, charities and other non-profit organizations.
  - Charitable gifts can reduce your estate tax.
  - Gifts can be designated for a certain purpose.
  - Gifts can be specific dollar amounts, or different dollar amounts based upon the size of your estate, or a percentage of your estate. For example:
    - $10,000 to [the charity of my choice]; or
    - $20,000 to [the charity of my choice] if my estate is at least $200,000; or
    - 10% of my estate to [the charity of my choice].

Last Will and Testament

- Executing your Will
  - You will need two witnesses who do not receive property under the Will.
  - A Notary Public will notarize your signature and those of the witnesses, creating a "self proving Will" so that the witnesses do not have to appear in court after your death to authenticate the Will.
- Safe Keeping of your Will
  - Only the original copy of the Will is valid.
  - Leave the original with the Probate Clerk at the county courthouse for a one-time fee of $2.00 in Virginia, and keep a copy for your records.

Financial Power of Attorney

- Durable General Financial Power of Attorney
  - Allows another person to take financial actions on your behalf.
    - Pay bills, open/close bank accounts, manage investments, sell real estate, etc.
  - May be effective immediately, or only when two doctors have determined that you are unable to make decisions on your own:
    - You are unable to understand your condition and make decisions.
    - You are in a coma or under anesthesia and can not make decisions.
  - "Durable" means that it is effective even if you are unable to understand or manage your own finances. Without the "Durable" distinction, the power of attorney is only good when you are competent to make decisions.
  - "General" means that it covers a wide range of circumstances, as opposed to a "Limited" power of attorney which may be for a specific transaction or period in time.

Financial Power of Attorney

- Choosing your Financial Power of Attorney Agent
  - Usually your spouse will be the first agent.
  - If your spouse is unable to serve as your agent, has predeceased you, or is not reachable, you will select one or more alternate agents.
  - Financial Power of Attorney Agents should be good with money, accounting and paperwork and should be trustworthy.
  - Your Financial Power of Attorney Agent does not have to be the same person as your Medical Power of Attorney Agent.

Advance Medical Directive/ Living Will

- Known as "Advance Medical Directive" or "Living Will" (both terms refer to the same document)
- Contains your wishes for your medical care in case you end up in a vegetative state:
  - Should food or water be given?
  - Should artificial respiration be used?
  - etc.
- Also may contain a directive on organ donation.

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Medical Power of Attorney

- "Medical" or "Healthcare" Power of Attorney
  - Allows another person to make health care decisions on your behalf.
  - May be effective immediately, or only when two doctors have determined that you are unable to make decisions on your own:
    - You are unable to understand your condition and make decisions.
    - You are in a coma or under anesthesia and can not make decisions.
  - Includes a HIPAA Release so that your designated agent can review your medical records.

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Medical Power of Attorney

- Choosing your Medical Power of Attorney Agent
  - Usually your spouse will be the first agent.
  - If your spouse is unable to serve as your agent, has predeceased you, or is not reachable, you will select one or more alternate agents.
  - Medical Power of Attorney Agents should be capable of making decisions under pressure, and should understand your wishes for your health care.
  - Your Medical Power of Attorney Agent does not have to be the same person as your Financial Power of Attorney Agent.

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Asset Protection and Estate Planning

Legal documents that every adult needs:

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- ✓ Durable Financial Power of Attorney
- ✓ Advanced Medical Directive/Living Will
- ✓ Medical Power of Attorney

Taxes, Trusts and Asset Protection:

- Gift and Estate Taxes for 2016 and beyond
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Tax Planning: Federal Estate Tax

- Federal Estate Tax
  - In 2016, the estate tax is:
    - $5.45 Million Tax Free (or $10.90 Million for a couple if Portability election timely filed)
    - Estate Tax Rate of 40% on amount over $5.45 Million
    - Unlimited spousal deduction for US Citizens.
  - In 2017 and subsequent years:
    - Tax free limit goes up with inflation each year.
    - Tax rate stays at 40% for any assets over the tax free limit.

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Tax Planning: Federal Estate Tax

- Federal Estate Tax
  - What is included in taxable estate?
    - Assets owned by the decedent which are included in probate,

    AND
    - Life insurance
    - Jointly owned property
    - Retirement accounts
    - Powers of Appointment
    - Annuities

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Tax Planning: State Estate and Inheritance Taxes

- Virginia
  - No estate or inheritance tax.
- D.C.
  - Estate tax of up to 16% on estates over $2M.
  - May increase to federal limit in 2018.
- Maryland
  - Estate tax of 9.9% - 16% on estates over $2M. (Legislation recently passed that will raise the floor to the Federal level of $5.43M by 2019).
  - Inheritance tax on bequests of over $1,000, except to relatives.

Tax Planning: Federal Gift Tax

- Federal Gift Tax
  - No tax on gifts of up to $14,000 per year to each individual allowed under the "annual exclusion."
  - No tax on lifetime gifts up to $5.45 Million, but these gifts reduce your Estate Tax exemption.
  - The best thing you can do for your beneficiaries is to make regular annual transfers to them during their lives, reducing your estate tax and benefiting them early.

Tax Planning: Asset Freezing Transactions

- Asset Freezing Transactions
  - By making a gift during your lifetime, either within the annual Gift Tax exclusion, or above the exclusion, utilizing your lifetime exemption or paying the tax, you shift assets and their appreciation to your beneficiaries.
    - Example: Transfer asset of $100,000 in Year 1. Asset appreciates at 7% per year. After 20 years, asset is worth $400,000.
  - Can be done in trust to control assets after the transfer is made.

Tax Planning: 529 Accounts

- College Savings (529) Plans
  - Each child may receive up to $350,000 in contributions during their life for a Virginia plan.
  - Contributions made in one year may be treated as spread out over several years to use the annual Gift Tax exclusion.
  - Funds grow tax free.
  - No tax is paid on funds used to pay for college or graduate school tuition, books and fees.
  - Credit for scholarships received by student.
  - Unused funds can be rolled over to other siblings.

Trusts

- A Trust is an instrument where legal title and beneficial ownership are split.
  - Trustee holds legal title.
  - Beneficiaries receive beneficial ownership.
  - Can have both current and contingent beneficiaries.
- Several types of Trusts:
  - Testamentary Trust, created by your Will.
  - Revocable "Living" Trust.
  - Irrevocable Asset Protection Trust.
  - Irrevocable Life Insurance Trust.

Testamentary Trust

- Created by your Will.
- Does not avoid costs or time of Probate.
- Less expensive and easier to set up.
- No management required during life.
- Not tax efficient for inheritance of retirement accounts.
- A sufficient "contingency plan" for young married couples with children.

Revocable “Living” Trust

- Avoids the expense and time of probate.
- More work to create than a Testamentary Trust.
- The Trust must be the **owner** or **beneficiary** of all of your assets to avoid Probate and to give Trustee control.
- You can be your own Trustee during your life.
- No tax consequences during your life.

Revocable “Living” Trust

- You can be your own Trustee during your life.
- Select Successor Trustees to take over if you become incapacitated or die.
  - Spouse
  - Children
  - Friends or other Family
  - Bank or Trust Company
  - Attorney

Revocable “Living” Trust

- Provides control for assets after death of one spouse and after death of both spouses.
- “See-Through” provisions allow for tax advantaged inheritance of retirement accounts.
- Spendthrift provisions can provide care for parents or beneficiaries with creditor or money issues.

Revocable “Living” Trust

- Special Needs Trust provisions can provide for disabled or incapacitated beneficiaries.
- Under Age Beneficiary provisions can provide for children, grandchildren, and other young beneficiaries.
  - Provide for education, living expenses, health care, etc. until the beneficiaries reach a designated age or finish college, etc.
  - Pooled vs. individual trust options.

Revocable “Living” Trust

- Can include bequests of money or tangible property for individuals or organizations.
- Can include charitable bequests, charitable lead or unitrust provisions, etc.
- Can include provisions for the care of pets.
- Duration is limited in most states by the Rule Against Perpetuities.
  - A life in being (measuring life) plus twenty-one years.

Revocable “Living” Trust

- When to use a Revocable Trust:
  - If you are not married, and all assets would go through probate.
  - Savings over going through Probate for estates with more than $100,000 - $200,000.
  - Avoid probate on real estate in multiple states.
  - Less hassle and time for your beneficiaries.
  - Tax advantages for retirement accounts and options for estate tax planning for estates with $1M or more.
  - Much easier for your successor trustees (children, etc.) to care for you if you become incapacitated during your life.

Revocable "Living" Trust Common Mistakes

- Client never funds the trust, so the estate still has to go through probate on death to fund the Trust.
- Client doesn't fund the trust correctly, so they end up paying a lot more taxes than necessary (e.g. with retirement accounts, etc.).
- Client funds the trust prematurely and loses some tax benefit (e.g. for those who are disabled and get property tax deductions).

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Revocable "Living" Trust Common Mistakes

- The Trust doesn't have the correct tax provisions to handle the assets for which it is the beneficiary (e.g. no "see-through" provisions for the Trust inheriting IRAs and using the beneficiaries as the measuring live for stretch-out, or the trust has a charity as one of the residuary beneficiaries, invaliding the whole see-through clause).
- The Trust does not have provisions for creditor protection or special needs beneficiaries.

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Revocable "Living" Trust Common Mistakes

- The Trust does not have a contingency plan for items that come up in the future, such as:
  - Settlor or a beneficiary moves to another state or country;
  - Last Trustee dies or resigns and there is no provision for a successor;
  - A Trustee who is also a Beneficiary has a power of appointment and can't appoint a co-trustee or special trustee to avoid a tax problem in their estate
  - And many more things with bad tax outcomes or which require expensive court orders to fix.

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Irrevocable Asset Protection Trust

- Created during your life.
- Best for retired age individuals with involved adult children as beneficiaries, who do not have long term care insurance, or who have limited duration long term care insurance.
- You can not revoke or amend the trust **without the permission of all beneficiaries**.
- Protects your nest egg from costs of long term care (e.g. nursing home), and from creditors.
- Revocable trust can be converted to an irrevocable asset protection trust if the need arises.
- Medicaid has a five year look back for transfers to trust.

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Irrevocable Life Insurance Trust

- Created during your life.
- Trust owns life insurance.
- Since the life insurance policy is not owned or controlled by the insured person, the proceeds from the life insurance pass **completely free of income, gift and estate tax** to your beneficiaries.
- You can not be your own trustee, but each spouse can be the trustee for the other spouse's trust.
- You can not revoke or amend the trust **without the permission of all beneficiaries**.
- Hedge against lower estate tax limit, higher rates.
- Strategy for reducing size of taxable estate.

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Tax Planning: Inherited Retirement Accounts

- Retirement accounts can designate beneficiaries directly, allowing beneficiaries to continue tax free (Roth) or tax deferred (Traditional) growth.
- If an estate is designated as beneficiary, which is the default for many plans if no beneficiary is designated or if there is no surviving spouse, then the account has to be cashed out, taxes paid, and tax deferral stops.
- A Trust can be named as beneficiary if it meets IRS regulations for "see-through" provisions, allowing control over the retirement account funds by your Trustee **and** continued tax deferral.

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Tax Planning: Inherited Retirement Accounts

- Inheritance by Spouse
  - Spouse can hold as their own retirement account, with no required minimum distributions (RMDs) until they reach retirement age.
  - TSPs have special rules about spouses inheriting.
- Inheritance by others
  - No penalty for early withdrawal.
  - Required minimum distributions (RMDs) start immediately but are measured by the life expectancy of the beneficiary.
  - If a pooled Trust is used, the beneficiary with the *shortest* life expectancy sets the RMDs for all beneficiaries.
  - If individual Trust shares are set up, each beneficiary uses their own life expectancy for RMDs.
- Double stretch out is possible with spouse then others.

Tax Planning: Roth IRA Conversions

- Roth IRA Conversions
  - Before 2010 there were limits on conversion and use of Roth IRA plans for individuals and couples with Adjusted Gross Income (AGI) over $150,000 per year.
  - Starting in 2010, anyone can convert a workplace or personal retirement account to a Roth IRA.
  - For 2011 and later years, taxes must be paid in the year in which the conversion takes place.
  - Conversions should be structured to:
    - Separate asset types (small, mid, large cap; stocks, bonds, etc.)
    - Allow for partial re-characterization of conversions so that conversion amount can be matched to income tax brackets in the year of conversion.
    - Allow for partial re-characterization of conversions for assets that have declined in value between conversion and tax filing.

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Arlington LAW GROUP

- Estate Planning:
  - We offer fixed price estate planning packages for individuals or couples at reasonable prices.
- Business Law:
  - We advise businesses and business owners during the whole lifecycle: formation of entities; business purchases and sales; general counsel services for contracts, commercial real estate, employment law, commercial disputes, etc. while running the business.
- Employment Law
  - Wrongful termination, discrimination, non-compete and employee contracts, and other employee issues.

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