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**PLANNING YOUR ESTATE -  
A STEP-BY-STEP APPROACH**

**By: Barry A. Nelson, Esq.**

**I. INTRODUCTION**

As individuals approach retirement age, the need has never been greater to have a complete estate plan overhaul. Unfortunately, many people tend to overlook this need. Consequently, when the first spouse passes away, needless turmoil is often a byproduct. This article, while most relevant to persons approaching retirement age, addresses certain steps that all individuals should consider when planning their estate.

**II. ESTATE PLANNING DATA SHEET**

One of the most important steps in planning an estate is completing an Estate Planning Data Sheet (the "Data Sheet"). In addition to including a list of the individual's assets, liabilities, income and expenses, the Data Sheet also provides the name of the individual's family advisors, such as accountant, insurance agent, investment manager, stock broker, trust officer, etc. The Data Sheet should also include the individual's preference method for burial and be kept in a place where family members can easily locate it. The preparation of a Data Sheet minimizes the confusion that otherwise occurs upon one's death. After all it is not uncommon to find a surviving spouse who is unable to locate the family checkbook. Data Sheets can be obtained by most estate planning attorneys and are often found in financial magazines.

**III. DO YOU NEED A WILL?**

**A. Non-Tax Issues**

Studies have found that as many as 30% of Americans die without a Will. It is not uncommon to find individuals who have the majority of their assets held jointly or in survivorship accounts who believe that a Will is therefore unnecessary. However, while each state has a statute specifying how probate property passes upon the death of an individual without a Will ("intestate"), the statute is not always consistent with the decedent's desires. Additionally, the disposition of non-probate assets such as bank accounts held in survivorship accounts (e.g., Barry in Trust for Samantha or, Barry or Samantha), upon a spouse's death is not always in accordance with what was anticipated. A Will is the only way to guarantee that probate assets will be distributed in accordance with one's desires, especially if certain unanticipated events occur. Example 1, below, highlights some of the shortcomings of using joint bank accounts to pass assets to family members upon the death of the initial account owner.

## EXAMPLE 1

Joan is a 70-year-old widow. She has three children, Moe, Larry and Curley all between the ages of 40 and 50. She has assets valued at \$300,000 (all in savings and brokerage accounts). Joan was told that she could avoid probate by putting all of her accounts in trust for her children (e.g., Joan's accounts are titled in the name of "Joan in-trust-for Moe, Larry and Curley"). Each of Joan's children has two children between the ages of 18 and 22.

Upon Joan's death, if her three sons were alive, they would each receive \$100,000. The money would avoid probate and pass by operation of law. However, if Moe predeceased Joan, most state laws would result in Joan's two surviving sons dividing the entire account upon Joan's death, and Moe's children would receive nothing. Unfortunately, it is more than likely that Joan would have wanted her two grandchildren, Moe's children, to share his \$100,000, rather than it pass to her other sons.

Even if Joan changed title to the account after Moe's death in order to add Moe's children, another problem would occur upon Joan's death. Assuming Moe's children are 18 and 22 at the time of Joan's death, then Moe's children would each receive \$75,000 outright and free of trust. Many parents would prefer that their children not receive an outright distribution until years later. It should be noted that under Florida law any life insurance proceeds, IRA benefits or jointly owned bank accounts in excess of \$5,000 that pass to a person who has yet to attain the age of 18 must be held subject to guardianship court supervision.

If we assume the facts of Example 1, above, except that Joan has a Will and the account is not held jointly, then the account would pass according to the terms of Joan's Will upon her death. Joan's Will could provide that in the event Moe predeceased Joan, Moe's children would inherit the share Moe would have received; provided, however that if any beneficiary under Joan's Will is younger than 25 years of age at the time a distribution to such beneficiary would be made (or any other age selected in the Will), the personal representative of the Will could delay the distribution to said beneficiary until the beneficiary reached 25 years of age (or whatever age selected). Until such time, the assets could be held in a trust created under Joan's Will for the benefit such beneficiary and the Trustee could pay to or for the benefit of such beneficiary such amounts as may be required for their health, education, maintenance and support. Any amount not distributed for such purposes could be distributed outright to such beneficiary when such beneficiary attains age 25 (or whatever age is selected in the Will).

### **B. Tax Issues**

#### **1. General**

The Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"), which President Bush signed on June 7, 2001, significantly changed the transfer tax system. EGTRRA increased the applicable exclusion amount and decreased the estate tax rates beginning in 2002. While the law did not eliminate the gift tax, it did lower gift tax rates and increase the gift tax applicable exclusion amount. In 2010, estate tax and generation skipping transfer taxes will be eliminated completely. However, beginning on January 1, 2011, the provisions "sunset" and are reinstated as if EGTRRA had never occurred. The chart below illustrates the changes brought on by EGTRRA.

Calendar Year	Highest Estate & Gift Tax Rate	Estate Tax Applicable Exclusion Amount	Gift Tax Applicable Exclusion Amount	GST Tax Rate	GST Exemption
2001	55% *	\$675,000	\$675,000	55%	\$1,060,000
2002	50%	\$1,000,000	\$1,000,000	50%	\$1,100,000**
2003	49%	\$1,000,000	\$1,000,000	49%	\$1,100,000**
2004	48%	\$1,500,000	\$1,000,000	48%	\$1,500,000
2005	47%	\$1,500,000	\$1,000,000	47%	\$1,500,000
2006	46%	\$2,000,000	\$1,000,000	46%	\$2,000,000
2007	45%	\$2,000,000	\$1,000,000	45%	\$2,000,000
2008	45%	\$2,000,000	\$1,000,000	45%	\$2,000,000
2009	45%	\$3,500,000	\$1,000,000	45%	\$3,500,000
2010	35% †	N/A	\$1,000,000	N/A	N/A
2011	55%	\$1,000,000	\$1,000,000		

\* 60% for amounts from \$10,000,000 to \$17,184,000

\*\* To be adjusted for inflation.

† Gift tax only

If a family's combined wealth (i.e., husband and wife) in 2007 fails to exceed \$2 Million, the family should generally not be concerned with federal estate taxes. This is because assuming both spouses die prior to 2009 when the applicable exclusion amount increases to \$3.5 million, the entire estate tax should be eliminated by the applicable exclusion amount of \$3.5 million. However, the applicable exclusion amount will be reduced by any taxable gifts previously made (i.e., gifts in excess of \$12,000 per year per beneficiary for 2007).

Life insurance proceeds must be included in the value of a person's taxable estate for federal estate tax purposes, if such person owns such policies individually or has certain rights over said policies, including the right to name the beneficiary of the policy. Additionally, the value of any retirement benefits (i.e., pension and profit sharing) payable as a result of such person's death must also be included in the value of the taxable estate.

If a family's combined wealth in 2007 exceeds \$2 Million, an estate tax projection should be prepared to determine the amount of estate taxes which would be payable upon the death of the first spouse and the surviving spouse under their current estate plan. It can then be determined whether the estate plan should be revised to permit both spouses to pass a total of \$4 million free of estate tax (assuming both spouses were to pass away prior to 2009) and increasing to \$7 Million (assuming both spouses survive until 2009). If both spouses were to die in 2010, their entire estate (even if their gross estate exceeds \$7 Million) would pass free of estate and generation skipping transfer tax.

If a family's combined wealth in 2007 exceeds \$2 Million, it generally is not advantageous to have the entire estate pass outright to the surviving spouse. While such a plan would not result in estate tax as a result of the unlimited marital deduction, the first spouse to die would waste his or her applicable exclusion amount. The net effect of such a devise is that fewer assets would pass estate tax free than if proper planning were initiated. Example 2, below, explains how additional estate taxes are likely to be incurred upon the surviving spouse's death, where as, they could have been avoided.

## EXAMPLE 2

Marty and Terry, his wife, have a net worth of \$4 Million, of which \$2 Million is held solely by Marty and \$2 Million is held solely by Terry. If Marty's Will provides an outright bequest of all of his assets to Terry, then as a result of the unlimited marital deduction, there will be no federal estate tax incurred in 2007 (Marty's assumed year of death). However, Marty would have wasted his \$2 Million applicable exclusion amount, which could otherwise have passed assets from his estate free of federal estate tax.

Proper estate planning could have placed Marty's \$2 Million applicable exclusion amount in a family trust upon his death (the "Family Trust") for the benefit of Terry during her lifetime, and thereafter to their children. If the Family Trust is properly drafted and administered in an arms-length manner, the value of the assets in the Family Trust would not be included in Terry's estate upon her death. Notwithstanding the fact that the Family Trust could provide Terry with the following benefits during her lifetime: (1) all of the income from the Trust payable annually; (2) any additional amount from trust principal that she may need for her health, education, maintenance and support; (3) the right to demand and be paid by the Trustee of the Trust the greater of \$5,000 or 5% of the value of the corpus of the Family Trust annually (non-cumulatively); and (4) a Special Power of Appointment (e.g., the power to designate among which of Terry's children and/or any qualified charities will receive the assets of the Family Trust upon Terry's death), the assets would not be taxed upon her death. Furthermore, in many states Terry could serve as sole trustee of the Family Trust even with the trust terms described above.

If Marty's Will provided for an outright distribution to Terry, rather than for a Family Trust, upon Terry's death her estate will include an additional \$2 million which could have passed free of estate tax with the planning described above (i.e., Marty's \$2 Million applicable exclusion amount passing in a Family Trust). If Terry were to pass away prior to 2009, as a result of the outright distribution she received from Marty, her taxable estate would be valued at \$4 Million, compared to \$2 if the Family Trust were established. The additional amount of estate tax that will be incurred as a result of the outright distribution to Terry (which would have been avoided with proper planning), but still may be reduced with post mortem planning techniques such as a disclaimer is approximately \$900,000.

### 2. If the Wills Take Advantage of the Applicable Exclusion Amount, Individuals Must be Cautious About Holding Substantial Amounts of Jointly Owned Property.

Problems may still occur even if an individual has a Will that takes advantage of both the applicable exclusion amount and unlimited marital deduction. Most Wills drafted for purposes of tax savings provide an amount equal to the applicable exclusion amount (currently \$2 Million and increasing periodically to \$3.5 Million by 2009) to pass with certain adjustments to beneficiaries other than the surviving spouse either outright or into a Family Trust similar to that described in Example 2, above. As was explained above, such planning generally results in no estate tax being paid upon the death of the first spouse. Additionally, the amount passing outright or into the Family Trust is not included in the estate of the surviving spouse upon the surviving spouse's death.

However, when the majority of a couples' wealth is owned jointly with right of survivorship (e.g., the family residence, bank accounts, stock certificates, etc.), those assets pass by operation of law to the surviving spouse, regardless of any contrary provisions in a Will. Consequently, if all or the majority of a husband's assets are owned jointly with his wife, even with a properly drafted Will, the Wife (assuming she is the surviving spouse) will receive a substantially larger share of the husband's estate than would be desired for purposes of minimizing estate tax.

3. Consider Splitting Up Jointly Owned Property - For Taxable Estates Each Spouse Should Have Separately Owned Assets.

If a spouse's Will provides for an amount passing into a trust similar to the Family Trust or outright to beneficiaries other than the surviving spouse, then certain jointly owned assets should be divided so that both husband and wife own enough assets in their own names to take advantage of their respective applicable exclusion amounts. For couples with a combined net worth of at least \$4 Million, each spouse should have at least \$2 Million of assets in their own name to take advantage of their applicable exclusions.

If assets are owned jointly instead of split, upon the death of the first spouse, assets will pass to the surviving spouse by operation of law, rather than utilizing the first spouse's applicable exclusion. If the assets are split so that each spouse owns assets in their own name, upon the first spouse's death, the applicable exclusion amount can be passed outright or in trust. Then upon the surviving spouse's death, the applicable exclusion amount can also pass outright or in Trust. As described in Example 2, above, a considerable amount of estate taxes can be saved if both spouses utilize their applicable exclusion amounts. By way of example, if the total combined wealth equals \$4 Million, all of which is held in the husband's name alone, or if all assets are held jointly and the wife passes away first, she would not have any assets in her own name to take advantage of her applicable exclusion amount. The husband would then have \$4 Million in his own name and can only take advantage of his \$2 Million applicable exclusion amount assuming he dies prior to 2007. The additional estate tax that is likely to be incurred as a result of the wife not taking advantage of her applicable exclusion amount could be as much as \$900,000.

4. Caution Should Be Exercised before Transferring Assets.

Estate planning attorneys frequently advise clients of the benefits of transferring assets between spouses so that each spouse has enough assets in his or her own name to take advantage of the applicable exclusion amount. Unfortunately, we hear "war stories" about situations where one spouse transfers assets to another spouse to take advantage of estate planning benefits and the other spouse takes the money and squanders it or separates from the spouse who transferred the assets. Therefore, the non-tax factors of transferring substantial sums of money between spouses must be considered before any transfers are made. Moreover, other non-tax considerations should be analyzed, such as the disadvantage of owning assets solely in one's own name if there is a possibility of a lawsuit. Accordingly, most professionals should consider the safest manner to title their assets taking into consideration estate and gift tax savings opportunities as well as asset protection objectives.

#### **IV. OTHER ESTATE PLANNING DOCUMENTS THAT SHOULD BE CONSIDERED**

##### **A. Revocable Inter Vivos Trust.**

A Revocable Inter Vivos Trust (also commonly referred to as a Living Trust) is an instrument that should be considered for at least two reasons. First, a funded Revocable Trust avoids probate. For example, if Jacob has assets of \$2 Million and transfers all of his assets into a Revocable Trust, then upon Jacob's death, the assets included in his Revocable Trust will not be included in his probate estate. As a

result, in certain circumstances probate fees can be saved. However, a Revocable Trust does not have any estate tax benefits that are not otherwise obtained by using a Will.

Second, a Revocable Trust also provides that in the event the person creating the Revocable Trust (the “settlor” or “grantor”) becomes incapacitated and is unable to take care of his or her financial affairs, the successor trustee named in the Revocable Trust (typically a family member or institutional trustee) will use the assets in the Revocable Trust in order to provide for the health, maintenance and support of the settlor.

The Revocable Trust should provide that upon the death of the settlor, the assets remaining in the Revocable Trust should be distributed to the settlor’s beneficiaries in a manner similar to the distributions that would be made using a Will. The settlor can be the sole trustee of the Revocable Trust during his or her lifetime or may serve with his or her spouse, a trusted friend, relative or family advisor or a financial institution.

Due to the probate avoidance benefits of a Revocable Trust and the fact that a Revocable Trust can provide for the maintenance of the settlor in the event of the settlor’s incapacity, thereby possibly avoiding the need to have a guardian appointed to take care of the settlor, a Revocable Trust should be considered by anyone in their retirement years. A typical estate plan using a Revocable Trust should also include a short Will (a “Pour-over Will”), which controls the distribution of any probate assets. Typically, the Pour-over Will provides that any probate assets would “pour over” into the Revocable Trust and would be distributed in accordance with the terms of the Revocable Trust.

#### **B. Durable Power of Attorney.**

A Durable Power of Attorney regardless of one’s age, but especially important as one approaches retirement age, should be included in everyone’s estate plan. The document provides that the person executing it (i.e., the principal) grants a person (i.e., the attorney-in-fact) the right to take various actions on behalf of the principal, such as the right to withdraw funds from bank accounts, sell stocks, sell real estate, sign tax returns, make gifts if advantageous for the principal’s overall estate plan, etc. Although a regular Power of Attorney terminates once the principal becomes incapacitated, a Durable Power of Attorney remains valid in most states until an action is initiated to have the principal adjudicated incompetent or until the principal dies.

#### **C. Death With Dignity Agreement.**

Many states, including Florida, have adopted statutes permitting individuals to direct through a written instrument known as a “Living Will” or “Death With Dignity Agreement,” for their life not to be prolonged artificially with the use of life support equipment or tubal feeding devices if the possibility for recovery is minimal. Consequently, every person should consider adding a Death with Dignity Agreement, Living Will or similar document to his or her estate plan.

#### **D. Irrevocable Life Insurance Trust.**

An Irrevocable Life Insurance Trust is a trust used to own a life insurance policy. It is used for purposes of excluding the life insurance proceeds from estate (and frequently generation skipping transfer tax). For example, if Ralph owns a \$1 Million life insurance policy individually and names his spouse as the beneficiary, then upon Ralph’s death, the \$1 Million of insurance is included in Ralph’s estate. However, his estate will also obtain a marital deduction for the amount passing to his wife. Accordingly, there is no increased estate tax upon Ralph’s death. However, Ralph’s wife now has an additional \$1 Million in her estate that will become subject to estate tax upon her death.

If Ralph's life insurance policy were owned by an Irrevocable Life Insurance Trust or if he transferred the policy to an Irrevocable Life Insurance Trust and survived for three years after the transfer, the \$1 Million life insurance benefit would be excluded from not only Ralph's estate but also from the estate of Ralph's wife. The Irrevocable Life Insurance Trust could provide that upon Ralph's death the insurance proceeds would be held for the benefit of Ralph's wife during her lifetime; and upon her death, the assets in the Irrevocable Life Insurance Trust could be distributed to Ralph's children. There are numerous complexities, but anyone owning significant sums of life insurance should discuss the benefits of an Irrevocable Life Insurance Trust with an estate-planning attorney.

## **V. DOMICILE**

Many persons of retirement age own more than one home, one of which is the principal residence and the other, which is the vacation home. As retirement looms ever closer, the amount of time spent at the vacation home similarly increases. By way of example, many persons from the northeast have vacation homes in Florida. Upon retirement, it is common that these people will maintain their personal residence in the northeast but spend an increasingly greater amount of time in their vacation home in Florida. Establishing residence in a state is important for purposes of obtaining the benefits of the state's taxes and liberal asset protection laws. As Florida has extremely favorable estate tax laws and does not have individual income tax, it may be advantageous, in many cases, to establish Florida domicile.

The steps to take in order to establish domicile in a particular state are beyond the scope of this article. However, anyone spending substantial amounts of time in two different states must consider whether it would be advantageous to change domicile. Furthermore, if it is unclear in which state one permanently resides, it is possible that numerous legal suits will be initiated in the various jurisdictions the individual had a residence, each claiming that the taxpayer was domiciled there. Accordingly, clearly establishing domicile in a state will avoid these problems.

## **VI. ESTATE TAX SAVINGS STEPS FOR WEALTHY INDIVIDUALS TO TAKE NOW**

### **Step One Annual Gifts of \$12,000**

Without question, anyone with substantial wealth should take advantage of an exclusion that allows gifts of \$12,000 per year to any beneficiary. In a second marriage, if one spouse has no interest in making gifts of his or her own property to the children of the other spouse, a "split gift" election is available whereby gifts of one spouse are treated as if made one-half by the other spouse, regardless of whether all funds came from one bank account. For example, a couple having a combined net worth of approximately \$5 million can pass approximately \$2.6 million to their children and grandchildren free of estate, gift and generation skipping-transfer taxes if they made gifts of \$12,000 per beneficiary to each of their 3 children and 8 grandchildren for a period of 10 years (disregarding any adjustment for inflation).

Many wealthy clients are reluctant to follow through with a continual gifting campaign, as they are concerned their children will waste the money regardless of the significant estate tax savings that are generated from such a gifting campaign. For those who are concerned that their beneficiaries are not mature enough to handle outright annual \$12,000 gifts, the gifts can be made into an irrevocable trust. The irrevocable trust is separate and unrelated to the revocable (living) trust.

A properly drafted irrevocable trust will qualify for \$12,000 annual gift tax exclusions, but will still permit the donor to restrict the beneficiary from obtaining mandatory distributions from the trust until a later date (at an age the donor believes appropriate as stated in the irrevocable trust document). Most estate planners suggest providing for mandatory trust distributions over at least 3 time intervals (e.g. 1/3 at age 30, 1/3 at age 35, and 1/3 at age 40). Using this technique limits the potential loss a naive

beneficiary may incur after he or she receives his or her first mandatory distribution and hopefully will serve as a learning process if the beneficiary does make an unwise investment. Surely the beneficiary will be more cautious when the next mandatory trust distribution is received. Until the beneficiary receives mandatory distributions, the Trustee can have discretion to invade the trust to provide for beneficiary's health, education or support for other broader purposes.

In addition to annual gifts of \$12,000 per beneficiary, each person can make an unlimited number of additional tax free gifts by paying for another person's (i) tuition paid to a qualified educational institution; or (ii) medical expenses, if paid directly to the qualified medical care provider. This frequently overlooked gift tax benefit oftentimes dwarfs the amount a parent, grandparent or other donor can gift to their intended beneficiaries. For example, a child attending Harvard University may have tuition bills of \$50,000 per year and medical expenses of \$3,000 a year. In addition the student's room and board could be \$15,000 per year. A grandparent or other donor could pay: (i) the child's tuition (\$50,000) directly to the college; (ii) medical expenses (\$3,000) directly to the medical care provider; and (iii) give the child an additional \$12,000 per year. All such gifts would be non-taxable if paid as described above. However, room and board (\$15,000) is not covered by the gift tax exemption whether or not paid directly to the educational institution. Code Section 529 Education Plans (the "529 Plan") should also be considered especially in light of EGTRRA's enactment that allows 529 Plan assets used to pay qualified education expenses to avoid all income tax on items such as interest, dividends and capital gains. 529 Plans also allow the donor to maintain significant control over the assets conveyed to the 529 Plan that otherwise would not be permitted if the assets were to be excluded from the donor's estate.

## **Step Two**

### **Large Gifts to Family Members Using Applicable Exclusion Amount**

Wealthy individuals should consider making additional taxable gifts of up to \$1 Million (\$2 Million if married) to their children and grandchildren, which should not require the payment of current gift tax under certain circumstances. Each person is entitled to a \$1 Million gift tax exemption for gifts made during life and a applicable exclusion amount of \$2 Million for gifts made at death. For example, Jim and Edith (married) own land in Naples, Florida, valued at \$3 million, which is rapidly appreciating. I advised them to gift \$2 Million of this property (i.e., \$1 Million each) into a trust entitled the "Naples Family Trust." The beneficiaries of this trust include Jim and Edith's children and grandchildren. The trust provides that no mandatory distributions will be made until the Naples real estate is sold.

Jim and Edith previously made no taxable gifts prior to the gift of the Naples land. As a result of their gift tax exemption, they did not have to pay any current gift taxes upon making this gift. The major benefit of such a gift is that even if the Naples property appreciates to \$5 million at the time Jim and Edith die, the total value of the gift for estate and gift tax purposes should be frozen at \$2 Million. Therefore, by making this gift while Jim and Edith are alive, they can save over \$900,000 million of additional estate taxes that otherwise would be incurred if they owned the Naples Property at their death and the property appreciated to \$5 million.

Obviously not everyone is in a position to make gifts of \$2 Million while they are alive. However, for those who can, the potential tax savings are substantial and these gifts should be considered. The gifts do not need to be made all at once, but can be made over a period of years. The best assets to gift are those having reasonably high tax basis but are anticipated to appreciate rapidly. However, the donor must be certain to understand that once the gift is made, any appreciation on the gifted assets is for the beneficiary and not for the donor.

## **Step Three**

### **Take Advantage of Existing Estate Tax Loopholes**

#### **A. Qualified Personal Residence Trust (“QPRT”)**

During 1988, the House of Representatives tried to close an Estate and Gift Tax loophole commonly known as a Grantor Retained Income Trust (“GRIT”) that could save wealthy individuals millions in estate taxes. In 1990, the GRIT door was closed and is now restricted to planning for remote family members (e.g., nieces and nephews not children or grandchildren). However, it is still possible to plan for family and non-family members with a personal residence, whether a primary home or vacation home. The Qualified Personal Residence Trust (“QPRT”) is a planning technique that should be considered for homeowners with personal residences that will likely continue to appreciate in value.

#### EXAMPLE OF USE OF QPRT FOR RESIDENCE

Jerry, a wealthy 65-year-old individual, has a waterfront house in South Florida. Currently his house is valued at \$1 million. Jerry is not ready to make an outright gift of his house to his children and grandchildren because he wants to retain the right to live in his house for about 10 years. Jerry agreed to establish a QPRT whereby he transferred title to his house into a trust and retained the right, for a period of 10 years, to live in the house. After 10 years the house will be distributed to Jerry’s children. Because Jerry retained the use of the house for 10 years the IRS allows Jerry to discount the value of the gift going to this trust. Assuming the gift was made in January, 2007, to a 10 year QPRT, the discount results in a gift of \$1 million being treated as if it was a gift of approximately \$239,920. Because Jerry made no prior taxable gifts he did not have to pay any gift tax when he created this trust. For the next 10 years, Jerry gets to live in the house, and after 10 years his children receive the house without any additional gift or estate tax assuming Jerry survives the 10-year term. Even if the house appreciates to \$5 million, Jerry should not have to pay any additional gift or estate taxes in this example, assuming he survives the 10-year term of the QPRT. The savings could be in the millions. If Jerry dies during the 10-year term, the house is brought back into his estate and the applicable exclusion amount he used when he made the gift is restored.

#### **B. Family Limited Partnerships.**

Although the IRS continues to attack Family Limited Partnerships (“FLPs”), FLPs continue to provide numerous benefits in the area of asset protection and estate planning. FLPs offer the possibility of centralized family wealth management (a single family advisor can hold a FLP account, rather than several accounts for various family members). They also provide parents with a certain level of control, either directly as general partner, or indirectly as officers of the corporate general partner. Gifts of limited partnership units can be made to family members taking advantage of annual exclusions as well as minority and/or lack of marketability discounts. If a person dies owning interests in an FLP, valuation discounts also may be available. Therefore, when properly planned including correct formation and a legitimate business purpose, FLPs are a great planning technique to minimize estate and gift taxes.

#### **C. Charitable Gifts.**

Whether gifts to charity are made outright during a person’s lifetime or under a Will or trust, they are all eligible for a charitable deduction. Gifts, which are made into a trust, may be structured with the charity receiving either a present or a future interest in the property donated to the trust. Charitable lead or

charitable remainder trusts are great estate planning techniques as they allow for valuable tax benefits; however, they are also estate planning tools that require careful individual financial planning. Charitable trusts created during the transferor's lifetime in which the transferor retains the interest, must be considered in light of the transferor's exposure to the income tax and alternative minimum tax.

#### **Step Four Consider Tax Traps**

The increasing importance of having an estate plan checkup similar to the way one would with their primary physician is exemplified by the story of Leonard and Ruth. Leonard, a U.S. citizen, is married to Ruth who moved to the U.S. from Canada 15 years ago. While Ruth has a "green card," she is not a U.S. citizen. As part of tax changes in 1988, the unlimited marital deduction is no longer permitted for non-U.S. citizen spouses (even if the spouse is a U.S. resident for immigration and/or income tax purposes). Now a trust referred to as a "Qualified Domestic Trust" must be utilized. The requirements for such a trust generally cannot be satisfied unless existing Wills and Trusts are modified. By immediately modifying their Will and Trust we were able to save Ruth and Leonard approximately \$500,000 in estate taxes that would otherwise have become payable shortly after Leonard's death.

#### **Step Five Creditor Protection**

The first step to planning an estate should be to consider the individual's potential exposure to creditors. This is especially important for doctors, lawyers, architects, developers and anyone else who has or intends to sell a business where personal liability may later become an issue. For example, if a wife has substantial assets and her husband is a brain surgeon with substantial potential malpractice liability, it would be better for the physician's wife to leave assets to the husband in a spendthrift trust along with insurance, rather than outright. The same techniques should be considered for any other potential inheritances by the doctor from his family. Otherwise, once the doctor inherits outright sums, such assets become immediately available to potential creditors.

#### **Post-Mortem Planning**

With proper planning, significant tax savings can be achieved even after death; however, such planning must begin almost immediately. Such post-mortem planning requires a thorough understanding of techniques including disclaimers, QTIP elections, the use of certain estate tax credits and certain other complex estate planning techniques.

### **VII. PLANNING FOR DISABLED BENEFICIARIES**

Families that have disabled or special needs beneficiaries (referred to hereinafter as a "Special Needs Beneficiary") should consider establishing a "Special Needs Trust." If a Special Needs Beneficiary receives an outright inheritance or gift in a trust which does not contain special needs provisions, such funds may result in disqualifying the Special Needs Beneficiary from any federal and other public assistance benefits that otherwise may be available. A Special Needs Trust specifically provides that the Trustee is to pay for the Special Needs Beneficiary's luxuries and for items not covered by public assistance, such as (i) speech, behavioral, music, occupational and other therapies for which no public or private funds are otherwise available; (ii) differentials in cost between housing for shared and private rooms in institutional settings or to allow the Special Needs Beneficiary to reside in a private residence along with one or more companions; (iii) travel, companionship and cultural matters; (iv) allowance for family members who wish to visit the Special Needs Beneficiary from time to time as determined by the Trustee; (v) purchase of equipment such as CD players, radios, televisions, VCRs, etc.; (vi) other similar expenditures for the benefit of the Special Needs Beneficiary. Only with careful and creative drafting can a family be assured that the Special Needs

Beneficiary will benefit from his or her gift or, inheritance, without being disqualified from public assistance programs.

## **VIII. CONCLUSION**

When considering whether to update an existing estate plan or create an initial estate plan, the question each individual should ask is whether he or she would rather leave their money to their family or to the IRS. Most individuals do not like to address estate planning for no one wants to confront the issues involved with dying, especially for those who are young and healthy. However, failure to plan now could result in significant estate, income and gift taxes as well as the foreclosure of current loopholes. With little investment of time, one can create a sound estate plan that is structured to provide maximum asset protection and distributions to heirs as well as minimizing estate taxes. If a current estate plan is limited to a Will and trust without considering the techniques described above, additional estate and gift taxes at rates of up to 45% could be incurred.

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