

Special Report: 2010

The Critical Year NOT to Die Without Estate Planning!

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Are you using the 2010 estate tax uncertainty as an excuse to procrastinate, to put off estate planning? Have you been thinking, or even saying, “*There is no reason to do anything now, since there is no estate tax there is nothing to gain from planning. Might as well save money on attorney’s fees!*” If so, you are being penny-wise and pound foolish. Your head is in the sand and you’re headed like sheep to the slaughter!

Some have suggested—tongue in cheek I hope—that 2010 is the year to die. But if you have not done planning that is based on current law, **2010 could be the worst possible year to die**. Waiting to see what Congress will do before you plan? I wouldn’t assume they will do anything! After all, the Democrats in Congress are increasingly gun-shy about passing “liberal” legislation, while the President seems firmly opposed to tax breaks for the “rich”—all they have to do is remain gridlocked and no tax law change will occur. We’ll be stuck with the status quo.

Estate planning has never been primarily about estate taxes anyway, but **this year makes tax planning more, not less, important than ever!** You should plan now so that **if by chance** you die this year, your family reaps a **huge windfall of benefits**; and if you live to next year, you’re prepared for the dramatic tax increase.

This report summarizes both the **tax and non-tax** reasons that you should definitely get serious about estate planning this year, and why you should work with professional advisors who are committed to regular, routine maintenance and updating of your plan **so you won’t get caught again** by unexpected changes in the law.

The Current State of [Estate Tax] Affairs

The estate tax status quo is this. In 2001 the Congress passed legislation by which the estate tax exemption gradually rose from \$675,000 to a peak of \$3.5 million, with a tax rate of 45 percent, then was completely “repealed” as of January 1, 2010. The gift tax exemption remains \$1,000,000 (i.e., you have to die to transfer more than \$1,000,000 tax free).

However, the 2001 legislation will “sunset” at the end of 2010, meaning the 2001 legislation will expire. As of January 1, 2011, without further action in Washington, the law as in effect prior to the 2001 legislation snaps back into place with an estate tax exemption of \$1,000,000. Thereafter, everything you own at death over \$1,000,000 would be taxed at around 45% to 55%.

There is no estate tax this year, so no estate tax planning is needed, right?

Wrong! First, political and legal analysts seem to agree that we might see a **retroactive estate tax imposed**, even after you die. Congress could pass a law in December

that says, “all deaths since January 1 are subject to tax on everything over \$XX.” Therefore, you need planning that will address the “what if there is a tax at my death” question, **even if it is enacted retroactively**. Otherwise, your family can end up owing a huge tax that could have been avoided.

Let’s do a reality check here: do you think the 2010 “repeal” will be extended beyond 2010? In other words, do you really think that there will be an act of Congress and a signature of the President, cutting taxes on large estates, i.e., for “the rich”? OK, I was just checking. So we can all agree that even if it is not re-imposed during 2010, there will be an estate tax imposed for deaths in 2011 and after. All we don’t know is whether it will be on estates over \$1,000,000 (as law currently says it will be) or some increased amount.

So given that fact, let’s look at the second tax planning issue. Many people are positioned so as to **waste a tax exemption and assure a large tax later**. This would happen one of two ways:

2010 Special Report: Don’t die this year without proper estate planning!

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1. **Joint tenancy** ownership of assets: A financial professional I heard the other day is advising married clients to hold assets as joint tenants with right of survivorship to best deal with the 2010 tax situation. A **very, very bad** idea, as you'll see.
2. Many couples have **outdated plans** that never anticipated a year of no estate tax. Wills or trusts often include formulas based on the applicable estate tax exemption in effect at death. Such formulas can work in reverse when there is no estate tax. As a result, when the first spouse dies, all assets pass to the survivor. The result is much like joint tenancy.

In either event, when the first spouse dies (assume husband for the illustration...it could be either) all assets pass to the wife. "So what's the problem, as long as at the death there is no tax?" you ask. Well, instead of taking advantage of the tax repeal window, your "plan" actually defers the **taxable event until the tax returns**.

Imagine you have a \$7 million estate. All assets are held in joint tenancy (or your wills or trusts that leave as much as possible to the survivor). Husband dies in 2010. Everything passes to the wife. No tax. She lives into 2011. She dies. **Everything in excess of \$1 million is taxed at around 50%. The IRS gets a cool \$3,000,000!**

The tragedy is this: **you could plan** so that if the first one dies in a year like 2010 the entire \$7 million estate would pass into a trust controlled by and for the benefit of the survivor to manage and use as needed. All \$7 million would be protected from lawsuits. And the assets of the trust would not be counted as part of the survivor's estate at death. If the survivor lives beyond this temporary repeal of the estate tax (i.e., you make it to 2011) no problem! The entire \$7 million, *plus any appreciation*, would pass **tax-free to the children**.

What about smaller estates? Even on a \$1,500,000 estate, planning that leaves "everything to spouse" would cost your heirs **over \$200,000** in taxes.

So let's just summarize: in this year of "unlimited estate tax exemption" and the "repeal of the estate tax" every couple who will leave \$1,000,000 or more to heirs (remember, it is not just their "probate estate" we are talking about, but their taxable estate, which includes annuities, IRAs, life insurance, etc.) should have an estate tax plan!

Capital Gain Tax Trap.

A **second tax trap** lies for the unwary, unplanned estate: capital gain taxes. If you die in 2010, your estate plan must provide for allocation of a limited "step up" in

basis on your estate. Otherwise, you will saddle your children with as much as **\$5,600,000 in taxable gain**...all of which could be avoided! This is



especially important again for a married couple. With capital gain tax rates set to go up in coming years, it would be truly tragic to miss the opportunity to avoid that tax altogether.

You must have planning in place before death to take advantage of the capital gain "step up," then have careful, professional help in the settlement of your estate in order to maximize the benefits of the current tax law. At 15% federal and 3% state, **failure to take advantage of the unique 2010 capital gain tax law could cost your heirs well over \$1,000,000.**

Summary of 2010

Estate Planning Tax Law Essentials

An effective estate plan—one that will accomplish maximum tax planning benefits—**must have an "if-then-but-and" approach!** It must cover

If there is no estate tax in effect on my death (and no such tax is retroactively applied!) **then** I want my estate divided and administered so as to maximize CAPITAL GAIN TAX reduction;

But I still want to assure that my spouse has the least possible likelihood of paying taxes when he or she dies, even if that is in a year when the estate tax is in effect;

And I want to make sure that while I am living, I can still easily adapt my plan to take advantage of new laws and opportunities that arise!

This is possible, even practical...or I wouldn't bring it up. Our clients are prepared for whatever happens!

Estate Planning Is Much More Than Taxes!

Remember, it's not all about taxes. Let's look at other reasons that are just as important in a "no estate tax" year as they would be in any other year. **Some of these may be even more accessible and beneficial in 2010** than they otherwise would or will be:

Property Disposition.

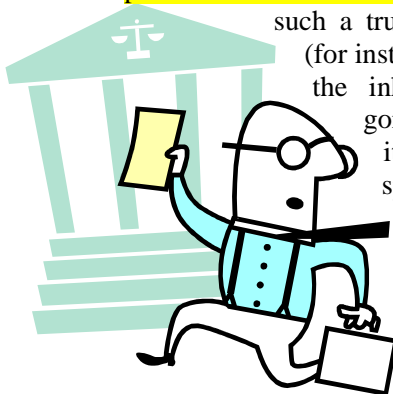
A primary focus of any comprehensive estate plan is the appropriate division and distribution of your property upon death. Does that need go away even if there were no estate tax? Of course not! If you fail to execute any type of estate plan, the State of Illinois has provided one, referred to as intestate succession law. However, this plan will almost certainly be contrary to your wishes. For example, if you're married with children and die, Illinois law gives half of your property to your surviving spouse and the other half divided among your surviving descendants.

The need to decide how and to whom you want your property to pass, and to **enact a plan to make that happen**, is necessary without regard to the estate tax.

Asset Protection for Heirs & Spouse.

(With tax benefits, too!)

Most of our clients have designed plans that deliver the family assets in what we call “**beneficiary-controlled**” trusts. One of the most powerful benefits of such a trust is the **protection that is afforded the assets** that are in



such a trust. While your daughter (for instance) controls her share of the inheritance (after you are gone, of course), can invest it as she sees fit, and can spend it as needed, the assets are safely **protected from claims of creditors, lawsuits, divorce and other “predator” attacks** that so often “wipe out”

hard earned and carefully accumulated assets.

A beneficiary-controlled trust can also be designed to **assure that a child’s inheritance—although available to her to spend as and when needed—does not increase her taxable estate**...an added benefit in today’s uncertain estate tax environment. After all, who knows whether there will be an estate tax in effect at the time of her death!

If your children are mature, careful adults who can handle their inheritance, you should consider designing such beneficiary-controlled trusts into your estate distribution plan while such planning is available!

A beneficiary-controlled trust is **not just for your children. If you are married, your first beneficiary who can receive such a trust would be your spouse.** A beneficiary-controlled trust for your spouse can be designed into the tax planning described on page 2!

On the other hand, perhaps you have one or more children who **could use some help** or guidance. Another powerful argument in favor of the use of a trust is the ability you have to set the terms of the distribution of the trust assets. Rather than an outright distribution of your estate to such a son, you could link his access to the trust property with certain life goals. For example, a trust could provide that he be given a right to receive the funds when he receives a college degree, remains employed for a certain time period, or attains certain income or business success. Such provisions could **provide an incentive** for him to further his education, work hard, or manage his own affairs well.

Alternatively, you could provide **disincentive** provisions that would stop access to an inheritance if a child engages in destructive behavior. Such planning can give you greater peace of mind that your hopes and goals for your children will be relevant after death.

Probate Avoidance

“Probate” used to have a reputation as being long, arduous, and costly. This reputation is not *always* deserved, but probate is typically a **more expensive way** to settle your estate than is trust-based planning. Don’t over-estimate probate avoidance, however! Every family is going to incur some legal, accounting, appraising and similar expenses in the settlement of an estate, even one that completely avoids probate.

You are undoubtedly aware of “beneficiary driven” investments that already avoid probate. However, when you try to avoid probate through beneficiary designations (or joint ownership of accounts and property) you are creating a stand-alone “plan” for each asset. This is hard to keep coordinated (and it creates more liability for your financial professionals). A living trust, with all assets properly titled to follow the trust, is much simpler to update whenever laws (*ahem*, weren’t we concerned about changing tax laws!) or your planning objectives change.

Remember, too, that while joint ownership of property and beneficiary designations may avoid probate at the death of the first spouse (although at the **risk of serious, future estate tax** as addressed on page 2), these mechanisms **generally will not avoid probate at the death of the surviving spouse** and still accomplish your division and disposition goals effectively.

Planning for Incapacity

Everyone should implement basic planning for incapacity, including the execution of powers of attorney for property and for health care. Living trusts allow for

greater specificity (answering the question, “How do I want my money managed and spent on me while I am disabled?”) with retained privacy. These documents, properly implemented and used, ensure that your financial matters can be attended to without the costly process of a guardianship proceeding and ensure that someone you trust is able to make critical financial and health care decisions.

Special Needs Planning.

As diagnoses of special needs (an individual who due to a mental, physical, or emotional disability is eligible for government benefits) increase, more families can benefit from proactive planning to provide funds for the benefit of the disabled individual without disqualifying them from receiving federal and state aid. This can be accomplished by creating a trust with provisions designed specifically for these purposes.



Let your professional advisors know whether any family members or other intended beneficiaries are disabled when you are designing your plan. Plan for it!

Creditor Protection for You.

Beneficiary-controlled trusts as described above can and should be routinely included in planning for your spouse and children, and will provide great creditor-protection advantages for them. On the other hand, creating creditor protection for your yourself is more limited.

Still, in the present planning environment there are many things you can do to create barriers to lawsuits and other predators that might appear in your life. We have outlined several “Asset Protection” methods on our website, which work effectively regardless of estate tax.

Does the lack of an Estate Tax mean you don’t care about your Minor Children?

Guardian Selection.

The need to name guardians of minor children is one of the first reasons you should seek estate planning advice. The importance of this issue does not diminish in an uncertain tax environment. If you have a will in place which names guardians, those names should be reviewed every few years. Not only will the minor children’s needs change as they age, but the financial, family, and health circumstances of the named guardian may change. Make sure you’ve **legally named the right people** for the **most important task that follows your death!**

Avoid Guardianship of Minor’s Estate.

When a minor child inherits property with a value in excess of \$10,000—even if that asset does not go through probate—a court will appoint a guardian to oversee that inheritance. This applies to the children who receive **life insurance and retirement plan** benefits. The appointment of a guardian and the related court oversight will drain resources from the child, since all costs associated with the administration of the guardianship estate and the legal representation of the guardian will be paid from the child’s assets.



It is preferable to avoid formal guardianship proceedings by providing in advance—**yes, planning ahead!**—for alternate methods of payment of the inheritance to a trust you create (within your estate plan) for the minor child.

Charitable Planning.

If you have charitable intentions and want to make gifts of some portion of your estate to charity, you must plan ahead, and carefully. Without clear direction in your will, trust or beneficiary designation, gifts to charitable organizations will not be completed upon the death of an individual.

Also, if you think you have a plan that already provides a charitable gift you’d better review your plan! Many charitable planning techniques included in wills and trusts are built around formulas that are tied to the estate tax exemption. If you die in 2010, your church or other charity might be disinherited, contrary to your intentions!

Plans That Work...People Who Care™

At **The Estate Planning Center**, we’ve been preparing our clients for years like this. Every year or two, our clients’ plans are updated. We are taking the “**if-then-but-and**” approach.

There is no reason to postpone planning. Rather, **plan so as to take advantage** of whatever tax opportunities exist!

All of our clients begin by attending an informative, no-obligation, 3-hour **Introductory Workshop**. Attendees are then provided a complementary appointment to discuss their situation further before any commitment can be made. Dates and times are on our website. Reservations are required, so give us a call so you can get your affairs in order...**ready for whatever** Congress might do...or not do!