GATEWAY FINANCIAL PARTNERS

Estate Planning Essentials

Overview

Discussing one's mortality is a topic that most people prefer to avoid, so they tend to put off estate planning. As uncomfortable as it may be, putting a solid estate plan in place will provide you with the peace of mind that comes with knowing that the wishes you spell out while you are alive will be followed to the letter upon your death. It is one last gift that you can leave to your heirs: a stress-free and cost-effective settlement of your estate.

Simply stated, if you have assets and property in your name, you have an estate. If you do not put pen to paper and engage a Trust and Estate Attorney to draft a Will for you, your state's Probate or Surrogate Court will determine who receives those assets upon your death. A Will is even more important for parents who have minor children. If you fail to determine who you want to be the legal guardian(s) of your children and something should happen to you and your spouse, the Surrogate Court will decide for you. In that case, the court will have no way of knowing what your intentions were.

Probate Process & Drawbacks

Probate is the legal process through which a deceased person's estate is administered and distributed. This process involves validating the deceased's Will, if one exists, and appointing an executor or administrator to manage the estate. The probate court oversees the payment of debts and taxes, and the distribution of the remaining assets to the rightful heirs.

Potential drawbacks of probate include:

- **Delays:** Probate can be a lengthy process, often taking several months to years to complete, depending on the complexity of the estate and any disputes that may arise.
- **Costs:** Probate can be expensive due to court fees, attorney fees, and executor fees, which can significantly reduce the value of the estate passed on to heirs.
- **Lack of Privacy:** Probate is a public process, meaning that the details of the estate, including assets and beneficiaries, become part of the public record.
- **Potential for Disputes:** The probate process can sometimes lead to disputes among heirs or beneficiaries, further delaying the distribution of assets and increasing costs.

So how can you ensure these potential problems do not impact you and your family? Here are strategies that can ensure your Estate Plan is both well-planned and well-executed.

Estate Planning: The Basics

Estate planning is the act of creating a plan while you are alive that clearly designates who receives your assets upon your death. There are many legal instruments utilized today.

WILL

A Will provides clear instructions on how your property is to be distributed upon your death. This document also establishes legal guardians for minor children. Your Will covers assets and property that are owned individually and do not have a named beneficiary. Such assets may include personal property (i.e. houses), your car, and business interests.

Many other types of assets will still be included in your estate but will pass outside the terms of your Will. For instance, your life insurance, 401(k) plan, and IRAs will have named beneficiaries, so these assets pass to the named person(s) without regard to your Will. Likewise, assets that are held jointly with your spouse pass to the surviving spouse by operation of law without regard to the terms of your Will.

Once a Will is probated, the cost of retaining an attorney to guide you through the court can be costly. In addition, once the contents of your Will have been probated, they are now in the public realm. The implication? Your relatives can ask to view the Will and potentially make claims on your assets.

Importance of Updating Your Will: It is crucial to regularly update your Will to reflect significant life changes such as marriage, divorce, the birth of children, or substantial changes in assets. Regular updates ensure that your Will accurately represents your current wishes and circumstances, preventing potential disputes and ensuring a smooth transition of your assets.

REVOCABLE LIVING TRUST

An effective way to avoid probate is to draft a Revocable Living Trust. Upon execution of the trust, your assets are now held in the trust while you are alive. The trust not only governs how your assets should be managed while you are living, but also designates to whom they should be distributed upon your death. Revocable Living Trusts generally cost more to draft than a Will. However, by avoiding probate, both the settlement and distribution of your estate remain private. In addition, the settlement period tends to be much shorter (and less expensive) than estates that need to go through the probate process.

Funding a Revocable Living Trust: To ensure that your Revocable Living Trust is effective, you must “fund” the trust by transferring ownership of your assets into it. This process involves changing the titles of your assets, such as bank accounts, real estate, and investments, to the name of the trust. Additionally, a Pour-Over Will can be used to transfer any remaining assets not included in the trust at the time of your death into the trust, ensuring that all your assets are managed according to your wishes.

IRREVOCABLE TRUST

Unlike Revocable Living Trusts, Irrevocable Trusts cannot be modified or terminated without the permission of the beneficiary. These trusts are often used to reduce estate taxes, protect assets from creditors, and provide for long-term care planning.

Irrevocable Trusts provide greater asset protection than Revocable Living Trusts. Once assets are in an Irrevocable Trust, they are no longer part of the grantor’s estate, reducing estate taxes and shielding them from creditors. This makes Irrevocable Trusts ideal for safeguarding wealth and planning for long-term care.

HEALTH CARE PROXY

Health Care Proxies allow you to designate a person who can make important medical decisions for you should you be incapacitated or unable to do so. The Health Care Proxy also includes your wishes as to whether you would like to receive life-sustaining procedures in an end-of-life, terminal condition. When selecting a health care proxy, choose someone you trust to make decisions in your best interest.

LIVING WILL

A Living Will, also known as an Advance Directive, outlines your wishes regarding medical treatment in situations where you are no longer able to communicate your decisions. This document can specify your preferences for life-sustaining treatments, resuscitation, and other critical care decisions.

A Living Will ensures your medical care reflects your wishes when you can't communicate. It guides healthcare providers and loved ones, reducing the burden of tough decisions and preventing unwanted treatments, while respecting your autonomy and dignity.

POWER OF ATTORNEY

A Power of Attorney allows you to delegate a person whom you trust to have access to and manage assets in your name.

Types of Power of Attorney:

- **Durable Power of Attorney:** This type of Power of Attorney remains in effect even if you become incapacitated. It allows your designated agent to manage your financial affairs without interruption.
- **Springing Power of Attorney:** This type of Power of Attorney only becomes effective under specific conditions, such as your incapacitation. It provides a safeguard by ensuring that your agent's authority is only activated when necessary.

BENEFICIARY DESIGNATIONS

Beneficiary designations are used to specify who will receive certain assets upon your death, such as life insurance policies, retirement accounts, and payable-on-death (POD) or transfer-on-death (TOD) accounts. These designations can help ensure that your assets are distributed according to your wishes without going through probate.

Beneficiary designations streamline the transfer of assets, ensuring they go directly to your chosen recipients without the delays and costs associated with probate. This helps maintain privacy and provides quicker access to funds for your beneficiaries.

Impact of Estate Taxes

Estate planning should include a strategy to avoid or reduce the potential impact of estate taxes on your estate. While federal estate taxes have become less of a concern for most Americans in recent years, they still affect some. The federal estate tax exemption has increased significantly—from under $1 million in 2001 to $13.6 million today. For married couples, the exemption is $27.2 million. As a result, fewer than 0.2% of estates are currently subject to federal estate taxes.

However, these tax laws are set to expire at the end of 2025, potentially reverting to lower exemption levels. This makes forward planning essential for protecting your estate from future tax liabilities. State-level estate and inheritance taxes can still apply depending on where you live. Currently, 18 states impose estate or inheritance taxes, with some states having much lower exemption thresholds than the federal level. For example, certain states may impose taxes on estates valued as low as $1 million or $2 million, significantly affecting the estate's value passed on to heirs. If you live in one of these states, it's important to understand both the exemption limits and any unique provisions, such as portability rules for spouses or "tax cliffs" that may increase the tax burden. Consulting with an estate planning professional can help you create a strategy tailored to your specific situation, ensuring that your estate plan is as tax-efficient as possible, no matter where you reside.

Common Strategies to Mitigate Estate Taxes

ANNUAL GIFTING

Annual gifts can be made to both children and grandchildren. The current gift tax annual exclusion amount is $18,000 per gift—or $36,000 per married couple. For example, if you and your spouse have two children, you can each gift $36,000 to each child for a total of $72,000 in gifts. There is no limit on the number of people to whom you may provide annual gifts.

CHARITABLE GIVING

Charitable gifts can reduce the value of your estate while also potentially lowering your taxes in the year that the gift is made.

IRREVOCABLE LIFE INSURANCE TRUST (ILIT)

ILITs can utilize life insurance proceeds to pay estate taxes. By placing a life insurance policy within an ILIT, the proceeds from the policy are excluded from the insured's taxable estate. This can provide liquidity to pay estate taxes without having to sell other estate assets, ensuring that the beneficiaries receive their intended inheritance.

GRANTOR RETAINED ANNUITY TRUSTS (GRATS)

GRATs allow you to transfer assets to beneficiaries while retaining the right to receive an annuity payment for a specified period. This strategy can help reduce the value of your taxable estate and transfer appreciation to your beneficiaries with minimal tax impact.

SPOUSAL LIFETIME ACCESS TRUSTS (SLATS)

SLATs are irrevocable trusts that allow one spouse to make a gift into a trust for the benefit of the other spouse, while also potentially benefiting other family members. This strategy can help reduce the taxable estate while still providing access to trust assets through the beneficiary spouse.

FAMILY LIMITED PARTNERSHIPS (FLPS)

FLPs allow you to transfer ownership of your business or other assets to family members while retaining control over the management of those assets. This strategy can help reduce the value of your taxable estate.

Summary

A thoughtful and well-crafted Estate Plan can provide you with peace of mind while saving time and money down the road for the people you love most. While most estate planning is not expensive, it does make sense to shop around as attorneys' fees for drafting and executing estate documents can vary significantly.

Beyond the cost, choose an attorney whom you trust and who is willing to spend the time with you to discuss the various options at your disposal. Federal tax laws are fluid and tend to change with Presidential administrations. Current tax laws expire at the end of 2025, so what works for you today might not work tomorrow. Once you have your plan in place, review it annually to make sure that it still reflects the current laws, your current situation, as well as your long-term wishes.

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