

Estate Plan Implementation and Post-Mortem Planning

Presented to:

The Financial Planning Association-Minnesota Chapter

April 15, 2008

Presented by:

Earl H. Cohen

Mansfield Tanick & Cohen, P.A.

A. HEALTH CARE DIRECTIVE (ADVANCE DIRECTIVE)– WILL THE CLIENT’S HEALTH CARE PROVIDER HAVE IT WHEN THEY NEED IT?

Completing a health care directive is an important first step, but it won’t do your client any good if it is not there when he or she needs it. DocuBank® and other national database service organizations can provide a solution for this problem.

DocuBank® is a service that, for a fee, will fax a client’s health care directive to a hospital at any time, anywhere in the world. Once your client enrolls in DocuBank®, they receive a DocuBank® card that should be carried with them at all times in their wallet, purse or somewhere easily accessible should the person become sick or injured and is unable to communicate or provide a copy of their advance directive. The card provides instructions to the medical provider to call DocuBank® and DocuBank® will then transmit the client’s health care directive to the medical provider. The card also contains emergency contact information, such as whether the client has any allergies, and whether they are an organ donor. In addition, the client’s attorney’s name may also appear on the card.

Informing your clients of services like DocuBank® can provide them with peace of mind in knowing that their health care directive will be accessible by their health care provider if it is ever needed.

B. THE KEY TO IMPLEMENTATION – ASSET RE-REGISTRATION

Many estate plans include trusts created to hold certain assets. Once the trust has been created, property with ownership documents must be re-registered in the trust's name. Unfortunately, people commonly delay or forget to re-register their assets under the name of the trust. Failure to re-register assets leaves them outside the trust and subject to probate and

possible unnecessary taxes. In addition, the chance that the property will go to the person or entity the grantor intended is reduced.

Therefore, as soon as the trust is established, the process of asset re-registration should begin. A new title document for each piece of property that transfers ownership into the trust's name is required. For real estate, a new deed showing the trust as the new owner must be prepared and recorded. For bank accounts, the financial institute should be able to provide a form to transfer ownership. The type of property owned by the trust which requires this re-registration of ownership includes:

- real estate
- bank accounts
- stocks and stock accounts
- money market accounts
- mutual funds
- most bonds, including U.S. Government Securities
- safety deposit boxes
- corporations, partnerships and limited partnerships
- cars, boats, motor homes and airplanes

Most of the steps necessary to re-register assets are fairly simple. Taking the time to re-register assets or to remind your clients do so, can ensure that the estate plan is carried out according to the client's wishes.

C. BENEFICIARY DESIGNATIONS

Beneficiaries are the individuals or entities that are designated to receive proceeds or assets under trusts, insurance policies, annuities and other important estate planning tools. These

proceeds or assets are non-probate assets that go directly to the beneficiary upon death, rather than through the probate process. Many clients do not understand that the proceeds of these assets will only go to the person or entity named as the beneficiary, even if the client's will names a different beneficiary they wish to receive the proceeds. Life changes such as a marriage, divorce, or death of a loved one can trigger the need to change beneficiary designations.

1. Primary and Secondary Beneficiaries

In addition to a primary beneficiary, an alternative or secondary beneficiary should also be designated who will receive the assets if the primary beneficiary is no longer living. If the client's primary beneficiary predeceases him or her, and no secondary beneficiary is named, state law will determine who gets the assets. If no beneficiary is named at all, the assets will go into the deceased person's estate, where they may be subject to negative tax consequences.

In choosing a beneficiary, it is also important to remember that minors, if named as beneficiaries of life insurance policies, retirement plans or annuities will require the appointment of a guardian or conservator. Preferably a trust would be established by the donor to manage the assets for the child's benefit until they reach the age of majority, at which time the assets can be distributed to the beneficiary.

Typically, it is a simple process to change a beneficiary designation and all that is needed to be done is to fill out a form, sign it and submit it to the appropriate entity. It is very important to remind clients to do this simple step to assure their assets are distributed as they wished.

D. USE AND MISUSE OF DISCLAIMERS

At the time of the estate planning, a client's estate may not be large enough to necessitate a "by-pass," or "credit shelter" trust to avoid the federal estate tax. If, however, the estate does

grow to reach the level of being subject to the estate tax at the time of the client's death, the beneficiary of the estate has the option under the Internal Revenue Code to "disclaim" any amount above the federal exemption under section 2518 of the Code and under Section 525.532 of Minnesota Statutes.

The disclaimant is treated, for estate and gift tax purposes, as though he or she never received any interest in the estate. See Treas. Reg. § 25.2518-1(b). Under section 2518(b)(4), a qualified disclaimer must pass without direction by the disclaimant to a person other than the disclaimant or the spouse of the decedent. If the disclaimant is the spouse of the decedent, he or she can allow their interest to pass into a trust set up for his or her own benefit.

Disclaimers allow a client to leave their estate to whomever they choose through his or her will, but the wills can also contain a clause providing that if their spouse disclaims the property, the property will pass into a trust for the benefit of the surviving spouse. Otherwise, if a beneficiary chooses to disclaim, the property will pass to the disclaimant's heirs as if they died intestate. Disclaimers are a useful tool in medium sized estates or smaller estates that may grow large enough to become subject to the estate tax.

The laws governing disclaimers must be followed closely. The Internal Revenue Code requires that the disclaimer meet requirements under the law of the state where the disclaimer occurs. Minnesota Statute section 501B.86 defines a disclaimer and sets forth the requirements that have to be met for a disclaimer to be qualified, which include:

- The disclaimer must be filed with the court.
- The disclaimer must be in writing.
- The disclaimant may not sell or otherwise contract to disclaim his or her interest to someone.

- The disclaimer must be done within nine months of the testator's death or within nine months of the event of transfer. If the disclaimer is done later than nine months, it will be treated as a gift and thereby subject to gift tax.
- The disclaimant may not be insolvent, or the disclaimer may be considered fraudulent.

Another important requirement is that there must be no acceptance of benefit by the disclaimer, i.e., a designated beneficiary cannot at first accept the benefit and then later decide to disclaim it, even if the beneficiary has used any of the benefit. However, there are two exceptions to this "hands off" rule:

- (1) the disclaimant may continue to live in a homestead while at the same time disclaiming his or her interest in the homestead to a credit shelter trust, and
- (2) in only situations where the disclaimant is the spouse, the spouse may disclaim his or her interest into a trust for his or her own benefit.

E. USE OF QTIPS TO SOLVE THE MINNESOTA AND FEDERAL ESTATE TAX EXEMPTION DIFFERENTIAL

The Internal Revenue Services imposes an estate tax on all property, real or personal, tangible or intangible, owned by decedent at the time of his or her death.¹ Minnesota also imposes an estate tax.² A certain amount of an estate may be set aside as exempt from the federal or state estate tax. The exemption for federal estate tax is currently \$2,000,000 and will rise to \$3,500,000 on January 1, 2009. The exemption for Minnesota estate tax is currently \$1,000,000. The remainder of the estate above the exemption amount is subject to the estate tax.

¹ I.R.C. § 2033, et. seq.

² Minn. Stat. § 289A, et. seq.

A Qualified Terminable Interest Property (QTIP) is an estate tax election that can be made for all or part of the estate property subject to estate tax, provided that the property may be classified as qualified terminable interest property.³ The Internal Revenue Code classifies property as qualified terminable interest property if: (1) the property is transferred by a spouse (the donor spouse) to his or her spouse; (2) the donor spouse has “qualifying income interest for life;” and (3) the spouse makes a QTIP election for the gift.⁴

The problem with having differing federal and state estate tax exemptions is that the client and estate planning attorney must decide if they wish to (1) fund a bypass trust with the full \$2,000,000 federal exemption, which in turn triggers Minnesota estate tax on the differential between the federal exemption and the state exemption, or (2) fund the bypass trust with just the amount exempt from Minnesota estate tax, \$1,000,000, thereby avoiding taxes upon the death of the first spouse but “wasting” half of the federal exemption amount?

Compounding the issue, the estate tax exemption is subject to change, with the federal exemption scheduled to increase to \$3,500,000 in 2009. Therefore, at the time the estate planning is done, it is not always possible to predict whether the client’s estate will be subject to estate tax at the time of the client’s death. The QTIP can be used to help solve this dilemma.

The client’s estate plan can be structured to include a provision permitting the trustee to set aside an amount equal to the estate tax exemption, as it exists as of the date of the client’s death. This provision provides clients with a great amount of flexibility in their estate planning. For instance, a client with an estate of \$3,000,000 would currently be subject to estate tax and may therefore want an estate plan that provides for a credit shelter trust funded with the full \$2,000,000 exemption. However, if the client dies in 2009 when the federal exemption reaches

³ I.R.C. § 2056, subd. b(7).

⁴ I.R.C. § 2523, subd. f(2).

\$3,500,000, the client's estate would no longer be subject to the federal estate tax. In this type of situation, the client may decide to forego choosing whether to fund the credit shelter trust with \$1,000,000 or \$2,000,000 now, and instead permit the trustee to pick the amount needed to fund the trust up to the amount exempt from state estate tax at the time of the client's death.

Because of the uncertainty in predicting a client's future estate worth and the changing estate tax exemptions, using a QTIP to help solve the differential between the Minnesota and federal estate tax exemption differential can provide a client with greater flexibility in his or her estate planning.

F. WHAT ABOUT A CHARITABLE PLAN?

Many clients, not just those who are significantly wealthy, may be good candidates for charitable giving, but do not realize it. While anyone can structure their estate plan to include charitable giving, those who may be particularly good candidates include clients who do not have any descendants, clients with significantly appreciated property, and clients with particularly large retirement accounts or life insurance policies.

There are many different ways to structure a charitable plan. Contributions can be made through:

- Outright donations;
- Bequests;
- Endowments;
- Charitable annuities;
- Charitable trusts: such as Charitable Lead Trusts and Charitable Remainder Trusts; and
- Life insurance.

In addition to the philanthropic rewards of giving, an estate plan that includes charitable giving can have financial benefits for both the client and the client's heirs including income tax, estate tax, gift tax deductions, and minimization of capital gains tax. Tax deductions can be affected by how much the client is donating, what kind of property the client is donating, whether the client is donating to a private or public charity. Many other issues, both financial and personal, may factor into choosing the charitable plan that is right for a client. Therefore, choosing a charitable plan is best made through consultation with an estate planning attorney and a tax advisor.