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ESTATE PLANNING DOCUMENTS OVERVIEW

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An estate plan benefits both you and your loved ones in the event of your incapacity and upon your death. Planning now, while you are healthy, enables you to choose appropriate fiduciaries to handle your affairs. Without such a plan in place, the court will appoint a conservator if you are incapacitated and will appoint an administrator upon your death. The court will also appoint guardians for your minor children.

By taking the time to plan now, you make these decisions yourself instead of leaving it up to the court. Moreover, you choose your beneficiaries instead of having the state determine them for you; you are able to plan the manner and timing of distributions to those beneficiaries; and you can avoid probate and minimize taxes. Thus estate planning has lasting benefits for both you and your loved ones. The documents most commonly used in estate planning, both basic and advanced, are described below.

I. BASIC ESTATE PLANNING

Generally, the documents comprising a basic estate plan are a revocable living trust, a pour-over will, an advance health care directive or health care power of attorney, a durable power of attorney for financial matters, and a Health Insurance Portability and Accountability Act authorization.

Revocable Living Trust

People often use a revocable living trust to avoid probate, for tax planning, and to control the manner and timing of distribution to beneficiaries. Unlike a will, which is a public document filed with the court, the trust is private. Property held in the name of the trust is not subject to probate proceedings.

You need to transfer your assets (e.g., real estate) into the trust, generally with the assistance of an attorney. You continue to control and manage the assets as you do now, but upon your incapacity, your named successor trustee manages the trust assets on your behalf without a court having to appoint a conservator. Upon your death, your successor trustee distributes the assets to your beneficiaries according to the terms of the trust.

Will

A “pour over” will is typically used in conjunction with a living trust, to catch any assets that may not have been transferred to the trust, so they can be distributed according to the trust’s terms. You also nominate guardians for your minor children in the will.

Durable Power of Attorney for Financial Matters

A Durable Power of Attorney for financial matters enables a designated individual to handle your non-trust assets (e.g., pay your bills from your checking account, transfer assets to your living trust) in the event you are incapacitated.

Advance Health Care Directive or Power of Attorney for Health Care

An Advance Health Care Directive allows you to designate an agent to make health care decisions for you in the event you are incapacitated. In addition to the release and execution of health care records and forms and consent to surgery and the like, it can be used to express your preferences regarding life-sustaining care.

Health Insurance Portability and Accountability Act Authorization

A Health Insurance Portability and Accountability Act ("HIPAA") authorization permits your designated agent to obtain protected medical information about you in order to handle your medical affairs.

II. ADVANCED ESTATE PLANNING

Larger estates; those in excess of the federal estate tax credit amount or applicable exclusion amount ($2 million per person in 2008, and $3.5 million in 2009) may benefit from one or more of the following strategies and associated documents, which can be used alone or in conjunction with the others.

Irrevocable Life Insurance Trust

There is a common misconception that life insurance proceeds are not subject to federal estate taxes. While the proceeds are free from income tax, they are countable as part of your taxable estate and therefore about half its value can be lost to estate taxes. An Irrevocable Life Insurance Trust (ILIT) is created specifically for the purpose of owning your life insurance policy. The ILIT holds the policy outside of your estate and keeps the proceeds from being taxable to your estate. The proceeds can then be used to provide your estate with the liquidity to pay estate taxes, pay off debts, pay final expenses, and provide income to a surviving spouse or children. You can use your annual gift tax exclusion to make cash gifts to your trust to pay the premium on the life insurance policy.

Qualified Personal Residence Trust

A Qualified Personal Residence Trust (QPRT) allows you to give away your house or vacation home at a discount, freeze its value for estate tax purposes, and still continue to live in it.

Family Limited Partnerships and Limited Liability Companies

Family Limited Partnerships (FLPs) and Limited Liability Companies (LLCs) are entities involving members of your family. The main advantages of forming and funding FLPs and LLCs involve estate and gift tax savings and asset protection.

Grantor Retained Trusts

A Grantor Retained Annuity Trust (GRAT) is an irrevocable trust to which you contribute assets. You retain the right to receive annuity payments for a specified period of time based on an assumed discount rate determined by the IRS. At the end of the term, assets in the trust pass to other beneficiaries. The GRAT provides gift and estate tax savings if the return on the assets placed in the GRAT exceeds the assumed discount rate. Grantor Retained Unitrusts (GRUTs), where distributions are based on a percentage of assets instead of an annuity, and Grantor Retained Interest Trusts (GRITs), where you retain an income interest, are similar techniques.

Intentionally Defective Grantor Trusts

Alternatively, you may want to sell assets to an Intentionally Defective Grantor Trust (IDGT), an irrevocable trust you establish that is excluded from the your estate for federal estate tax purposes, yet owned by you for income tax purposes. The sale can be in exchange for a promissory note. Similar to a GRAT, the sale of the promissory note provides gift and estate tax savings if the return on the IDGT exceeds the interest rate on the note.

Charitable Planning Documents

If you are charitably inclined and seeking to minimize taxes while enhancing the amounts going to your loved ones, you may want to consider charitable planning. Documents associated with charitable planning include Charitable Remainder Trusts (CRATs and CRUTs), Charitable Lead Trusts (CLATs and CLUTs), and Private Foundations.

In preparing any of the foregoing documents, it is important to work with a qualified attorney because the law in this area is very specialized, changes often, and involves complex tax matters. The ramifications for you and your loved ones can be far-reaching, both emotionally and financially.