Insight on Estate Planning

April/May 2012

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Estate Planning Pitfall

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We welcome the opportunity to discuss your needs and help you meet your estate planning and wealth transfer objectives.

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Make health care decisions while you're healthy

Estate planning isn't just about what happens to your assets after you die. It's also about protecting yourself and your loved ones. This includes having a plan for making critical medical decisions in the event you're unable to make them yourself. And, as with other aspects of your estate plan, the time to act is now, while you're healthy. If an illness or injury renders you unconscious or otherwise incapacitated, it will be too late.

Without a plan that expresses your wishes, your family may have to make medical decisions on your behalf or petition a court for a conservatorship. Either way, there's no guarantee that these decisions will be made the way you would want, or by the person you would choose.

2 documents, 2 purposes

To ensure that your wishes are carried out, and that your family is spared the burden of guessing — or arguing over — what you would decide, put those wishes in writing. Generally, that means executing two documents: 1) a living will and 2) a health care power of attorney (HCPA).

Unfortunately, these documents are known by many different names, which can lead to confusion. Living wills are sometimes called "advance directives," "health care directives" or "directives to physicians." And HCPAs may also be known as "durable medical powers of attorney," "durable powers of attorney for health care" or "health care proxies." In some states, "advance directive" refers to a single document that contains both a living will and an HCPA.

For the sake of convenience, we'll use the terms "living will" and "HCPA." Regardless of terminology, these documents serve two important purposes: 1) to guide health care providers in the event you become terminally ill or permanently unconscious, and 2) to appoint someone you trust to make medical decisions on your behalf.

Living will

A living will expresses your preferences for the use of life-sustaining medical procedures, such as artificial feeding and breathing, surgery, invasive diagnostic tests, and pain medication. It also specifies the situations in which these procedures should be used or withheld.

Living wills often contain a do not resuscitate order (DNR), which instructs medical personnel to not perform CPR in the event of cardiac arrest.

HCPA

An HCPA authorizes a surrogate — your spouse, child or another trusted representative — to make medical decisions or consent to medical treatment on your behalf when you're unable to do so. It's broader than a living will, which

Health insurance for your finances

If you're injured or become seriously ill, your health is the top priority. But it's also important to have a financial management plan in place in the event you become incapacitated. There are three traditional techniques for protecting your finances:

1. Joint ownership. Holding title to assets jointly with a family member or trusted friend is the simplest way to provide for their management in the event you're incapacitated. But this strategy has negative gift and estate tax implications and gives your co-owner unfettered access to your property even while you're in good health.

2. Durable power of attorney. This document appoints a representative to manage your investments, pay your bills, file tax returns and otherwise handle your finances under conditions you define and subject to limitations you establish. In many states, durable powers of attorney take effect immediately, but some states allow "springing" powers, authorizing your representative to act only if you are incapacitated.

3. Living trust. By placing your assets in a living trust (also referred to as a "revocable trust") and naming yourself as trustee, you retain complete control over your finances. If you become incapacitated, your chosen successor trustee takes over.

generally is limited to end-of-life situations, although there may be some overlap.

An HCPA might authorize your surrogate to make medical decisions that don't conflict with your living will, including consenting to medical treatment, placing you in a nursing home or other facility, or even implementing or discontinuing life-prolonging measures.

Maintain flexibility

It's a good idea to have both a living will and an HCPA or, if allowed by state law, a single document that combines the two. A living will typically details the procedures you want and don't want under specified circumstances. But no matter how carefully you plan, a document you prepare now can't account for every possible contingency down the road.

That's where an HCPA comes in. Although an HCPA can include specific instructions, it can also be used to provide general guidelines or principles and give your representative the discretion to deal with complex medical decisions and unanticipated circumstances (such as new treatment options).

This approach offers greater flexibility, but it also makes it critically important to appoint the right representative. Choose someone whom you trust unconditionally, who is in good health, and who is both willing and able to make decisions about your health care. And be sure to name at least one backup in the event your first choice is unavailable.

Put your plan into action

No matter how carefully you plan, living wills and HCPAs are effective only if your documents are readily accessible and health care providers honor them. Store your documents in a safe place that's always accessible and be sure your loved ones know where they are. Also, keep in mind that health care providers may be reluctant to honor documents that are several years old, so it's a good idea to sign new ones periodically.

In this digital age, you should also have an electronic copy available. Even though some jurisdictions may be hesitant to accept anything short of an original signature, a PDF of the document may in fact be sufficient.

Which planning strategies should unmarried couples implement?

Married couples have available to them greater (and more advantageous) estate planning options than unmarried couples. Yet unmarried couples face many of the same estate planning concerns as married couples. So they must engage in special planning to ensure that their decisions regarding asset distribution and health care are carried out per their wishes.

Employing workarounds

Because, depending on the state, state intestacy laws may offer no protection to an unmarried person who wishes to provide for his or her partner, it's essential for unmarried couples at minimum to employ a will or living trust.

In addition, federal law and the laws of many states don't recognize same-sex marriage. Plus, even if a couple lives in a state that recognizes same-sex marriage, they may own property in a state that doesn't recognize their marriage. Or, they may move to such a state. So married same-sex couples need to plan accordingly. That is, when considering the tax implications, they should plan as if they were unmarried — at least for federal purposes.

There are several estate planning challenges that unmarried couples must plan around, such as:

The marital deduction. Estate planning for married couples often centers on the marital deduction, which allows one spouse to make unlimited gifts to the other spouse free of gift or estate taxes. Unmarried couples don't enjoy this advantage; thus, lifetime gift planning is critical so they can make the most of the lifetime gift tax exemption and the $13,000 per recipient annual gift tax exclusion.

Tenancy by the entirety. Married and unmarried couples alike often hold real estate or other assets as joint tenants with rights of survivorship. When one owner dies, title automatically passes to the survivor. In many states, a special form of joint ownership — tenancy by the entirety — is available only to married couples. In addition to survivorship rights, tenancy by the entirety offers protection against claims by the spouse's individual creditors. Unmarried couples who seek greater protection against creditor claims should consider placing assets in a trust.

Will contests. Married or not, anyone's will is subject to challenge as improperly executed, or on grounds of lack of testamentary capacity, undue influence or fraud. For some unmarried couples, however, family members may be more likely to challenge a will simply because they disapprove of the relationship.

Unmarried couples should consider reducing the risk of such challenges by ensuring that their wills are carefully worded and properly

executed. They also should consider using separate attorneys, which can help refute charges of undue influence or fraud.

Health care decisions. A married person generally can make health care decisions on behalf of a spouse who has become incapacitated by illness or injury. Unmarried partners cannot do so without a written authorization, such as a living will or health care power of attorney. A durable power of attorney for property may also be desirable, allowing a partner to manage the other's assets during a period of incapacity. (See "Make health care decisions while you're healthy" on page 2 and "Health insurance for your finances" on page 3 for more information.)

Using a GRIT

There is one significant estate planning opportunity that gives unmarried couples an edge over married couples: a grantor retained income trust (GRIT). With a GRIT, one partner transfers assets to an irrevocable trust for the other's benefit. By retaining income and certain other interests in the trust the grantor minimizes its value for gift tax purposes.

Because state intestacy laws may offer no protection to an unmarried person who wishes to provide for his or her partner, unmarried couples should employ a will or living trust.

So long as the grantor survives the trust term, a GRIT has the potential to transfer substantial amounts of wealth tax-free, which led Congress in the late 1980s to eliminate these tax benefits for intrafamily transfers. But unmarried couples and other "nonfamily" members can still take advantage of this powerful estate planning strategy.

Achieving your estate planning goals

If you and your partner are in a long-term relationship but don't plan to marry or your marriage isn't legally recognized, there are specific strategies you can use to achieve your estate planning objectives. Your estate planning advisor can help you identify and implement those strategies.

Due diligence required when taking charitable deductions

Estate planning and charitable planning often go hand in hand. For many people, leaving a legacy of philanthropy is as important as providing financial security for their families. If your estate plan includes charitable contributions, be sure you understand their tax implications. The availability of income tax deductions for lifetime donations affects a contribution's cost and, therefore, the amount you can afford to give without jeopardizing your other estate planning goals.

One important requirement for charitable deductions is that the recipients of your largesse be organizations that are eligible to receive deductible contributions. These include qualified public charities, schools, museums, churches, certain supporting organizations and private foundations. To ensure that your contributions are deductible, it's critical to monitor the tax-exempt status of the organizations you support.

Check the list

Generally, the easiest way to check whether an organization is likely eligible for tax-deductible contributions is to make sure it's listed on IRS Publication 78. Publication 78 also indicates whether a listed organization is a public charity or a private foundation. This is significant because income tax deductions for contributions to private foundations are subject to lower percentage-of-income limits than contributions to public charities.

Another option is to consult the IRS Business Master File (BMF). In fact, if you're donating to a private foundation, the BMF is preferable because, unlike Publication 78, the BMF indicates whether a public charity is considered a "supporting organization."

To maintain their tax-advantaged status, private foundations that make grants to certain supporting organizations must exercise "expenditure responsibility," which means monitoring how the supporting organization receiving the grant spends the foundation's funds and ensuring the funds are used as intended. So an added benefit of reviewing the BMF is that this may give you peace of mind that your contribution will be used for what you intended.

Watch out for revocations

Just because an organization is listed in Publication 78 or the BMF, however, doesn't necessarily mean that it's currently eligible to receive tax-deductible contributions. An organization's tax exemption can be revoked.

For example, an organization's tax-exempt status is revoked automatically if it fails to file an annual information return (the Form 990 series) for three consecutive years. There's a bit of a lag from the point of revocation to the time the organization is removed from the lists.

If an organization's status is revoked for such failure to file, will you lose your tax deduction? Perhaps. The organization may correct the deficiency, however, by filing the required returns.

Further, under recently updated IRS rules, it has been clarified that, if an organization loses its tax-exempt status, contributions or grants to the organization are still allowable provided the donor 1) is unaware of the revocation and 2) makes the contribution or grant *before* the IRS makes a public announcement that the organization no longer qualifies.

Just because an organization is listed in Publication 78 or the BMF doesn't necessarily mean that it's currently eligible to receive tax-deductible contributions.

Generally, these announcements are made on the IRS website and in the Internal Revenue Bulletin. But they may also be published "by such other means designed to put the public on notice of the change in the organization's status."

Do your homework

To ensure that your charitable contributions are tax-deductible, check to see whether potential recipients are eligible and remain in good standing with the IRS *before* you get out your checkbook. It's also a good idea to document the steps you take to confirm an organization's status — such as checking Publication 78 and the IRS website — to protect yourself in the event of an IRS challenge.

Estate Planning Pitfall

A trust is the beneficiary of an IRA or retirement plan

If you own an IRA or participate in a qualified retirement plan such as a 401(k), it's possible to have the assets distributed to a trust when you die. As illustrated in a recent IRS private letter ruling (PLR), however, to preserve your retirement account's tax-deferral benefits, it's critical to properly designate a trust beneficiary.

If certain requirements are met, the trust beneficiary will be considered the retirement account's designated beneficiary, and required minimum distributions (RMDs) from the account can be stretched over the trust beneficiary's life expectancy — or, in the case of multiple beneficiaries, over the oldest beneficiary's life expectancy. If the requirements aren't met, the entire account balance will have to be distributed in a relatively short time.

IRS regulations state that a trust beneficiary qualifies as a designated beneficiary of an IRA or qualified plan if:

- The trust is a valid trust under state law (or will be after it's funded),
- The trust is irrevocable (or will become irrevocable at death),
- The beneficiaries with respect to the trust's interest in the retirement account are identifiable from the trust instrument, and
- Appropriate documentation has been provided to the plan administrator.

The PLR involved a married couple whose estate plan included several trusts, one of which was named beneficiary of the husband's IRA. Unfortunately, at the time of his death, the trust — and, therefore, the IRA — didn't have a designated beneficiary. The couple's children, as trustees, obtained a state court order allowing them to modify, or "reform," the trust to designate a beneficiary.

But the IRS refused to apply the terms of the reformed trust retroactively for federal tax purposes. Although the IRS will respect such state court orders when reformation is specifically authorized by the Internal Revenue Code, that was not the case here. The result: The husband's IRA was treated as having no designated beneficiary, accelerating distribution of the IRA balance.

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Comprehensive Estate Planning Services

Founded in 1960, Weinstock, Manion, Reisman, Shore & Neumann offers estate planning, probate and trust administration, general business and corporate law, taxation, real estate, and estate and trust litigation services. Because 12 of our 15 attorneys are actively involved in estate planning, we specialize in helping clients meet objectives like these:

- Dispose of assets in a tax-efficient manner by using revocable living trusts.
- Minimize estate taxes by using sophisticated lifetime giving techniques, such as Grantor Retained Interest Trusts and Charitable Remainder Trusts.
- Provide liquidity and save estate taxes by using life insurance and irrevocable life insurance trusts.
- Efficiently administer probate and trust estates.
- Transfer business interests to younger family members in a tax-efficient manner.
- Minimize generation-skipping transfer tax on transfers to grandchildren and great-grandchildren.
- Implement deferred compensation and qualified retirement plans, including pension and profit sharing plans.
- Reduce income and estate taxes on the receipt of benefits from retirement plans.
- Avoid court intervention if disability strikes.
- Maximize employee productivity through the use of stock options and other incentive programs.
- Dispose of business interests among co-owners.
- Save on income taxes, both now and in the future.
- Select and form business entities, such as corporations, limited liability companies and family limited partnerships.
- Protect the interests of beneficiaries or fiduciaries in estate, trust or conservatorship matters.

The professionals at Weinstock, Manion Reisman, Shore and Neumann bring over 300 years of combined experience to the services we provide. The stability of our firm enables our lawyers to work closely together with business specialists to give clients outstanding individualized attention.

Many of our lawyers are instructors at UCLA Extension and highly sought after as speakers for professional organizations in the community. Because we are at the forefront of current developments in law, we excel in designing strategies which help clients balance their business and financial interests with their personal and professional objectives in order to preserve and transfer their wealth.

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