Insight on Estate Planning

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Estate Planning Pitfall
You haven't reviewed your trusts this year

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

Please call us at 310-553-8844 to let us know how we can be of assistance.

Is your estate plan bulletproof?

Techniques for avoiding litigation over your estate

An inherent problem with wills and other estate planning documents such as trusts is that, when the time comes to put them into action, you won't be around to explain or interpret them. Fortunately, there are strategies you can use during your lifetime to minimize the risk of a fight over your estate after your death.

Treat heirs fairly

If someone succeeds in getting your will or trust thrown out in court, your estate will be distributed as if you had no will or trust — that is, according to the laws of intestate succession. The more closely your will or trust follows those laws, the less your heirs have to gain by contesting it. So, for example, an effective defensive strategy might be to provide equal shares for your children (including stepchildren). And if there's a deceased child, shares would be divided among his or her children.

Treating heirs equally can be a safe strategy for many families, but it can backfire when there are children from multiple marriages. Suppose your daughter from your current marriage is a college student and you have a financially independent son from a previous marriage. If you treat them equally, your daughter, who likely needs more financial help, may view your plan as unfair.

Explain yourself

You may have sound reasons for treating heirs unequally or leaving a substantial amount of your wealth to charity. Perhaps you follow Warren Buffet's philosophy that the right amount to leave your kids is "enough money so that they . . . feel they could do anything, but not so much that they could do nothing."

To avoid disputes or disappointment, it's wise to explain your reasoning to the family during your life.

Sell a family business to your child

Say you own a family business and want to leave it to your son John, who works in the business

The no-contest clause: Making it work

A no-contest clause — which disinherits an heir or beneficiary who unsuccessfully challenges a will or trust — can be a powerful disincentive to litigation over your estate plan. You don't need a no-contest clause for each person you name in your will or trust, but only for people who have the right to contest it — namely, those who would have received a share of your estate in the absence of a will or trust, such as your spouse or children.

To discourage heirs from contesting the estate plan, it's important to leave them *something*. If you leave them nothing, they'll have nothing to lose by challenging your plan. Instead, leave them an inheritance that's substantial enough to make them think twice before rocking the boat.

Be sure to check state law before using a no-contest clause. These clauses are allowed in most states, but some states limit them to certain types of challenges or require specific language for a clause to be effective.

with you. If you're concerned that your other children may object, consider selling the business to John during your life.

It's more difficult for siblings to challenge a lifetime sales contract than a bequest in a will. There are several techniques available — such as installment sales and sales to intentionally defective grantor trusts — that allow you to spread the payments over many years and minimize the tax impact.

Make disinheritances explicit

There's a reason it's called "writing someone out of your will." If you simply leave a child out, for example, he or she may contest your will, claiming the omission was an oversight. But if you spell out a disinheritance in writing, your intentions will be clear. Keep in mind that the laws in some states make it difficult to disinherit a child or spouse.

If someone succeeds in getting your will or trust thrown out in court, your estate will be distributed as if you had no will or trust — that is, according to the laws of intestate succession.

Be cautious when providing reasons for disinheriting someone. For example, if you state that you're disinheriting a child because he or she is "financially independent," you may open the door to litigation over the meaning of that term. And some reasons may violate public policy, such as disinheriting a child who marries outside the family's religion.

Preempt challenges to your mental capacity

Will contests often involve claims of undue influence or lack of testamentary capacity. There are

several techniques for avoiding these challenges, such as obtaining a written evaluation by a physician or psychiatrist and choosing witnesses who can attest to your mental capacity and are expected to be alive when you die.

Another option is to videotape the execution of your will. But this approach can backfire. For example, if you're nervous in front of the camera, your discomfort may be misinterpreted as duress or confusion.

Appoint a professional

Many people name a trusted child or friend as executor or personal representative of their estate or trustee of their trust, but this can sometimes lead to abuse-of-power claims. You can reduce the likelihood of these disputes by appointing an independent professional, such as a bank, an attorney or an accountant.

A professional executor, personal representative or trustee offers the added advantage of financial expertise and experience handling estates.

Get professional help

These are just a few examples of the many strategies you can use to "bulletproof" your estate plan. Your estate planning advisor can help you design a plan that achieves your goals while minimizing litigation risks. ∎

A good reason to revisit your estate plan

Accounting for digital assets

Have you accounted for any "digital assets" in your estate plan? Digital assets may include online bank and brokerage accounts, digital music, book collections, and photo galleries. If you own a business, your company's website, domain name, client and other databases, and electronic invoices are considered digital assets.

If you die without addressing these assets in your estate plan, your loved ones or other representatives may not be able to access them without going to court — or, worse yet, may not even know they exist.

Virtual documents in lieu of hard copies

Traditionally, when a loved one dies, family members go through his or her home to look for personal and business documents, including tax returns, bank and brokerage account statements, stock certificates, contracts, insurance policies, loan agreements, and so on. They may also collect photo albums, safe deposit box keys, correspondence and other valuable items.

Today, however, many of these items may not exist in "hard copy" form. Unless your estate plan addresses these digital assets, how will your family know where to find them or how to gain access?

Suppose, for example, that you opened a brokerage account online and elected to receive all of your statements electronically. Typically, the institution sends you an e-mail — which you may or may not save — alerting you that the current statement is available. You log on to the institution's website and view the statement, which you may or may not download to your computer.

If something were to happen to you, would your family or executor know that this account exists? Perhaps you save all of your statements and correspondence related to the account on your computer. But would your representatives know

where to look? And if your computer is password protected, how would they get in?

Even if your family knows about a digital asset, they'll also need to know the username and password to access it. If they don't have that information, they'll have to get a court order to access the asset, which can be a time-consuming process — and delays can cause irreparable damage, particularly when a business is involved. If your representatives lack access to your business e-mail account, for example, important requests from customers might be ignored, resulting in lost business.

Revealing your digital assets

The first step in accounting for digital assets is to conduct an inventory, including any computers, servers, handheld devices, websites or other places where these assets are stored. Next, talk with your estate planning advisor about strategies for ensuring that your representatives have immediate access to these assets in the event something happens to you.

Although you might want to provide in your will for the disposition of certain digital assets, a will isn't the place to list passwords or other confidential information. For one thing, a will is a public document. For another, amending the will each time you change a password would be expensive and time consuming.

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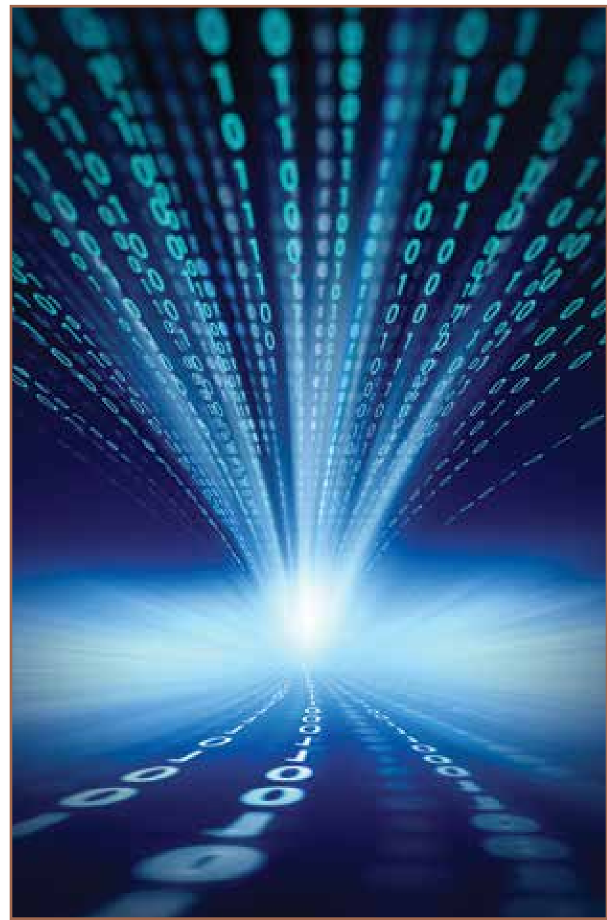
One solution is writing an informal letter to your executor or personal representative that lists important accounts, website addresses, usernames



and passwords. The letter can be stored in a safe deposit box, with a trusted advisor or in some other secure place. However, the problem with this approach is that you'll need to update the list each time you open or close an account or change your password, a process that's cumbersome and easily neglected.

A better solution is to establish a master password that gives the representative access to a list of passwords for all your important accounts, either on your computer or through a Web-based "password vault."

Bring your estate plan into the 21st century

Even though you can't physically touch digital assets, they're just as important to include in your estate plan as your material assets. Your estate planning advisor can help you account for any digital assets in your estate plan. ∎

Making gifts still matters, even after ATRA

The American Taxpayer Relief Act of 2012 (ATRA) eliminated much of the uncertainty that plagued estate planning for years by making two key provisions "permanent": the $5 million gift and estate tax exemption (adjusted annually for inflation) and exemption portability between spouses. Currently, the inflation-adjusted exemption is $5.25 million.

ATRA relieves some of the pressure on people to transfer wealth during their lives. But lifetime gifting still provides some significant advantages.

Tax savings for the affluent

If your net worth is large enough for estate taxes to be a concern, you'll still benefit from lifetime giving strategies designed to remove assets from your estate in a tax-efficient manner. And even if your estate is within the exemption amount, it's possible that it'll grow beyond that amount in the future. Gifting assets now — either outright or in trust — can "freeze" their value and remove future appreciation from your estate.

In addition, all things being equal, paying gift tax is "cheaper" than paying estate tax. Why? Because gift taxes are computed on a "tax-exclusive" basis while estate taxes are computed on a "tax-inclusive" basis. Here's an example:

Mary is in the top gift and estate tax bracket (currently 40%) and has already used her $5.25 million exemption. She'd like to make a $1 million after-tax gift to her daughter, Jane. If she makes the gift this year, it will cost $1.4 million — $1 million for the gift and $400,000 in gift tax.

If, instead, Mary decides to leave Jane a $1 million after-tax bequest, it'll cost $1.67 million (assuming the tax rate is still 40% when she dies) — $1 million for Jane and nearly $670,000 in estate taxes. The difference is that, with a bequest, estate tax applies to the amount used to pay the tax on the gift, as well as the amount of the gift itself.

Keep in mind that gifting is advantageous only if you survive for at least three years after you make a gift. Otherwise, the gift will be subject to the "three-year rule," which pulls assets back into your estate if they're transferred within three years before death.

Insurance against future tax changes

When it comes to taxes, "permanent" is a relative term. ATRA's estate tax law changes are permanent in that they aren't scheduled to expire after a certain period of time. But there are no guarantees Congress won't reduce the exemption — or increase rates — in the future in an effort to boost tax revenues.

An effective strategy for insuring yourself against future tax hikes is to take advantage of lifetime gifting to remove wealth from your estate under current, favorable conditions. *Nontaxable* gifts are particularly valuable because they aren't subject to the three-year rule. They include annual exclusion gifts — up to $14,000 per recipient this year ($28,000 for gifts by married couples) — as well as direct payments of tuition or medical expenses on behalf of your children or other beneficiaries.

Taxable gifts — including gifts within the $5.25 million exemption — are also effective. But there's a potential risk of estate tax exposure if you die within three years and the exemption is reduced.

A holistic approach

Don't make estate planning decisions based on tax savings alone. If lifetime gifting strategies are consistent with your overall estate planning objectives, they'll continue to offer significant tax benefits. Talk to your estate planning advisor to learn more about the estate tax implications involved with making gifts.

Estate Planning Pitfall

You haven't reviewed your trusts this year

If your estate plan includes one or more trusts, it's a good idea to review them in light of recent tax law changes. Higher income taxes — on individuals as well as trusts — may lead you to rethink the way your trusts are structured.

This year, several tax hikes take effect for "high earners." They include:

- A top income tax rate of 39.6% (up from 35%) on taxable income above $400,000 for single filers ($450,000 for joint filers),
- A 20% rate (up from 15%) on long-term capital gains and qualified dividends for taxpayers in the top bracket, and
- A new 3.8% tax on some or all net investment income for taxpayers with modified adjusted gross income over $200,000 for single filers ($250,000 for joint filers).

Trusts are also subject to these tax increases, but the income threshold is only $11,950 in 2013. With a *grantor* trust, you're treated as the owner for income tax purposes, even though your contributions are considered "completed gifts" for estate tax purposes. So you avoid the low trust threshold for these tax hikes. In addition, by paying the income taxes, you allow the trust to grow tax-free, leaving more for your heirs. And you can sell assets to the trust without tax consequences.

Despite these advantages, if tax hikes on your own income will be a burden, you might consider converting a grantor trust to a *non*grantor trust to shift tax liability to the trust. You can reduce the tax bite on the trust by 1) shifting trust assets into tax-exempt or tax-deferred investments, or 2) distributing trust income to beneficiaries in lower tax brackets. (Generally, trusts are taxed only on *undistributed* income.) But you should weigh potential tax savings against the benefits of keeping assets in the trust — including creditor protection and wealth preservation.

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Comprehensive Estate Planning Services

For over 50 years, the attorneys and staff of Weinstock Manion have focused on providing personalized, high-quality counsel to moderate to high net worth individuals, real estate investors, business owners, charitable organizations, beneficiaries and fiduciaries in the following practice areas:

- Estate Planning
- Wealth Transfer Planning
- Estate and Trust Administration
- Estate and Trust Litigation
- Business Succession Planning
- Charitable Planning and Family Foundations

Working with our client's other trusted advisors, our team of specialized attorneys and paralegals create and implement comprehensive, creative and practical estate plans with the goals of maximizing wealth transfer in accordance with our clients' wishes and reducing taxation.

Estate and trust administration can have significant financial consequences for both current and future beneficiaries. In an effort to minimize income and estate taxes, while maximizing estate and trust income for beneficiaries, our process involves an extensive amount of collaboration between our estate planning, taxation and transactional attorneys.

Weinstock Manion's litigators represent both fiduciaries and beneficiaries in estate and trust disputes. Our litigators are skilled at handling claims for breach of fiduciary duty, beneficiary disputes, disputes regarding the validity of wills and trusts, undue influence and all aspects of conservatorships and guardianships.

For many clients, ensuring the future of their family business through a well-structured succession plan is an essential component of their estate plan. Our team of transactional, tax and estate planning attorneys work with our clients' other trusted advisors to develop plans for retirement, management transition and liquidity events.

Supporting charitable causes is important to many of our clients. We help our clients support the causes they are passionate about in a tax-efficient manner through thoughtful charitable planning, including the creation of family foundations.

At Weinstock Manion, we understand that significant wealth can lead to complex personal and financial issues that may result in family conflict. Our goal is to help implement wealth transfer plans that minimized potential conflicts while promoting enduring legacies for generations to come.

We invite you to explore our team and services, and to contact us to learn more about how we may collaborate to preserve your legacy.

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