Planning for a Single Person

BASIC ESTATE PLANNING ARRANGEMENTS *EVERYONE* NEEDS

Estate planning seminars and articles often dwell on strategies pertinent to married couples and give relatively short shrift to unmarried individuals. Yet estate planning is just as important for single individuals, and perhaps even *more* important because there is no spouse to carry on and no easy strategy to defer estate taxes.

This Monograph is intended to provide an overview of estate planning for single individuals and to stimulate thinking before or after you meet with your attorney. We will begin with a brief discussion of the *need* for estate planning, describe the basic estate planning arrangements that *everyone* should have in place, provide an overview of the federal estate tax and planning strategies to minimize its impact, and finally, suggest a two-phase approach to estate planning.

THE NEED FOR ESTATE PLANNING

Every individual needs certain basic estate planning arrangements to provide for contingencies that may occur, and, in the event of the individual's death, to dispose of his or her property, minimize estate taxes, and provide for loved ones. Such arrangements typically include various kinds of insurance to ease the financial burden of life's contingencies, Durable Powers of Attorney and a Health Care Directive (or "Living Will") to provide for financial management and health care decision-making if the individual becomes disabled, and a Will or Revocable Living Trust to dispose of his or her property at death.

Unless appropriate arrangements have been implemented, state law dictates who will make decisions upon an individual's incapacity and who will inherit the individual's possessions. If an individual becomes unable to manage his or her affairs, the courts may appoint a guardian for the individual's person or property to make health care or financial decisions for the individual. When the individual dies, Washington state law determines how the individual's property is apportioned among relatives, and does so in a mechanical fashion without regard to the individual's desires, often triggering significant unnecessary estate taxes and expense. The object of estate planning is to ensure that an individual's personal desires are carried out, with minimum estate taxes and expense, leaving nothing to the discretion of the legislature or the courts.

THE BASIC ARRANGEMENTS *EVERYONE* NEEDS

There are certain "foundational" estate planning arrangements that every Washington resident should have in place, regardless of his or her circumstances. These include Durable Powers of Attorney for Financial Matters and Health Care Decisions and a Health Care Directive (or "Living Will") to provide for management and health care decisions if the individual can't manage for himself or herself, and an appropriate Will or a Revocable Living Trust to control the ultimate disposition of his or her property at death. Most individuals also need to review and coordinate the ownership and titling of their significant assets. If an individual owns any life insurance, annuity contracts, or retirement plans or IRAs, the individual should review the beneficiary designations that govern disposition of such assets because such assets are *not* ordinarily controlled by the individual's Will or Living Trust. Next, if an individual has (or might have) a taxable estate at death,[1] estate taxes and strategies to minimize estate taxes should be understood and considered. Finally, some individuals may want to consider their need for supplemental medical and/or long-term care insurance. Each of these topics is discussed in detail below.

DURABLE POWERS OF ATTORNEY- FINANCIAL & HEALTH CARE DECISIONS

In Washington, as in most states, if an individual becomes legally incompetent and unable to make decisions concerning his or her own property or medical care due to injury, illness or old age, the courts may appoint a guardian of the individual's estate or

1 As of January 1, 2015, individuals owning property with an aggregate value equal to $2.0 Million or more must file a Washington State estate tax return and are subject to Washington State estate tax on the value in excess of $2,054,000 at rates up to 20%. The amount of the federal estate tax exemption is $5.43 Million and the value in excess of such amount is taxed at a rate of 40%.

person to make required decisions. Guardianship proceedings may be embarrassing and expensive, and may result in a management and oversight procedure that may or may not be what the affected individual would have chosen for himself or herself.

To avoid such a judicially-imposed solution if the need arises, every individual should anticipate the possibility of incompetency and sign a Durable Power of Attorney, authorizing a trustworthy individual of his or her own choosing (the "Attorney in Fact") and probably one or more alternates to handle financial management and personal and health care decisions if the need arises.[2]

Durable Powers of Attorney take many different forms. Most individuals give the Attorney-in-Fact broad authority to take *all appropriate actions* incident to ownership and management of the individual's assets. Such authority should *include* authority to sell assets and reinvest the proceeds, file tax returns, receive funds from third parties, and even make tax-saving gifts up to the annual exclusion amount (currently $14,000 per year) to the individual's intended beneficiaries. However, in all but extraordinary circumstances, the Power of Attorney should not include the authority to change the individual's Revocable Living Trust or change beneficiary designations with respect to life insurance, annuities, and retirement plan accounts.

A Durable Power of Attorney may take effect *immediately* or only *in the future* upon a written determination that the individual has become incompetent by his or her regular physicians (a "springing power of attorney"). Since the objective is generally only to avoid guardianship proceedings if the individual becomes incompetent, so-called "springing powers of attorney" are popular because they provide safeguards that the powers will not be used unless the individual cannot act on his or her own. Individuals who have more immediate needs for the appointment of an agent, but who are not yet incompetent, may prefer powers that take effect immediately.

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[2] Sometimes single individuals, acting on bad advice, add the name of an adult child or other "helper" to accounts in the erroneous belief that this is the way to authorize a helper to pay bills, manage investments, etc. Sometimes the helper is merely an authorized *signer* on the account but other times the individual makes the helper a *co-owner*. Joint ownership arrangements sometimes override the individual's Will, and not infrequently lead to disputes over whether the decedent intended merely to authorize the helper to assist in managing his or her finances, or intended to make a testamentary gift to the helper. In most circumstances, we recommend use of a Durable Power of Attorney to authorize a helper to manage assets rather than signatory, co-ownership or survivorship arrangements.

Obviously, the Attorney-in-Fact should be competent and trustworthy, and should live in Washington. Often, an individual designates the same persons who will act as Personal Representative and Trustee under the Will or Living Trust. Ultimately, the Attorney-in-Fact is accountable to the individual, the Personal Representative of the individual's estate, and the estate beneficiaries. As such, the attorney-in-fact may be liable for misdeeds or neglect.

HEALTH CARE DIRECTIVE (OR "LIVING WILL")

In addition to a Power of Attorney authorizing a trusted family member or friend to make medical decisions if the individual is unable to participate in his or her own care, most individuals in Washington should sign, or at least consider, a Health Care Directive or so-called "Living Will". This instrument is the device by which an individual directs his or her doctor concerning continuation of medical care if he or she develops a terminal medical condition or is permanently unconscious and recovery is not expected. Washington does not permit euthanasia or "assisted suicide", but it permits individuals to express their desires concerning continuation of medical treatment under such circumstances. If an individual has signed a Living Will, and if the individual's family and physicians can agree that recovery is hopeless, treatment may be halted.

WILL OR REVOCABLE LIVING TRUST

For most individuals in Washington, a Will is the basic estate planning vehicle.[3] An individual's Will appoints a "Personal Representative" (or "Executor") to settle the individual's estate and controls disposition of the individual's property. A Will can provide for outright disposition to family, friends or charity, or it can establish trusts for

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[3] While Wills remain the most popular basic estate planning vehicle for Washington residents, Revocable Living Trusts have become popular alternatives, and the complexity and cost of legal proceedings to settle an estate (known as *probate*) in some states has made Living Trusts the preferred vehicle in those states. Revocable Living Trusts may not be necessary (or even particularly advantageous) for most Washington residents but individual circumstances often make a Living Trust worth considering. The advantages and disadvantages of using a Revocable Living Trust rather than a Will as the basic estate planning vehicle are set forth in a separate S&Z Monograph entitled ***"REVOCABLE LIVING TRUSTS: Does a Trust Make Sense for You?"***

beneficiaries. In addition, if the individual has minor children, the Will appoints a guardian for such children during their minority.

PROVISIONS FOR DESCENDANTS

Individuals with children or grandchildren frequently desire to leave all or a substantial portion of their assets to their descendants. The Will may provide either for *outright* distribution to descendants or for assets to be left in trust, as appropriate. If children are relatively young, disabled or simply immature, a Will typically provides for a designated third party (the "Trustee") to hold and manage property for the benefit of the children until the beneficiaries reach maturity or until the disability subsides. There are several alternative approaches to structuring such a trust, depending on the circumstances and objectives of the parent.

a. A Common Pot Trust to be Divided at a Future Date. If the parent's resources are limited and the children are relatively young, it usually makes sense for the Will to establish a "common pot trust" for *all* of the children, and direct the Trustee, in its discretion, to distribute or expend funds from the common pot equally or unequally to meet each child's respective needs until the youngest attains some specified age of maturity (e.g. college graduation age). At that point, the trust might be *divided* equally or unequally into "separate share trusts" for the respective children but continued for their respective benefit until each child reaches some older specified age of maturity. For example, an individual with two youngsters ages 12 and 13 might provide for a "common pot trust" until the youngest reaches age 22, at which time the pot trust will be divided into "separate share trusts" for each. Following division, the Trustee would distribute or expend income and/or principal of each separate share trust as required to meet the respective child's support,

Estate Planning Ideas

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medical and educational needs (and perhaps even to help buy a house or get started in business).

b. Separate Share Trusts. If the parent's estate is plentiful or the children are grown (or nearly so), it may make more sense for the Will to establish a separate share trust for each child immediately upon the parent's death, and direct the Trustee to distribute or expend funds from each share to or for the respective child's benefit as required. Where trust funds are adequate for all, this approach may make equitable administration and accounting easier, and there may be a small income tax advantage to this approach.

c. Staged Distributions. Whether the Will provides for a common pot trust for all of the children or a separate share trust for each child, it often makes sense to provide for ultimate distribution of each child's trust principal to him or her at *several* different points in time rather than all at once. For example, a parent's Will might provide that if trust funds are not exhausted sooner, the Trustee must distribute one-third (1/3) of the trust principal held for each child outright to him or her at age 25, one-third (1/3) at age 30, and the balance at age 35. Such "staged distributions" enable children to gain experience managing assets before *all* of the assets come into their possession. Hopefully, if a child handles the initial distribution badly, he or she may be a little smarter five years later when the second installment is received.

d. Lifetime Trust. The Will could alternatively provide that the trust continues for the lifetime of the beneficiary. Often, when such a trust is elected, the mature child beneficiary will become trustee of his or her own trust, providing the beneficiary with protection from marital and other creditors and sometimes providing tax savings to that and future beneficiaries [5]

e. Alternative Provision for a Deceased Child's Descendants, Siblings or Others. Obviously, the Will should address the possibility that a child may die before receiving his

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[5] While trusts *always* make sense for minor or immature children, trusts also make sense for responsible, adult children who will be successful in their own right since a trust can protect a child's inherited assets from potential marital claims and creditors' claims as well as future estate taxes. The advantages of using trusts specially designed to optimize each beneficiary's control, benefit and flexibility are described in a separate S&Z Monograph entitled ***"GENERATION-SKIPPING TRUSTS: The Best Way to leave property to Successful Adult Children".***

or her entire trust share, and appropriate provision should be made for a deceased child's descendants and/or alternative disposition.

PROVISIONS FOR OTHER FAMILY MEMBERS & FRIENDS

If an individual wants to leave all or a portion of his or her property to other family members, the most appropriate approach depends upon the circumstances and objectives of the individual and the circumstances of the recipients. The Will may provide for *outright* distribution to recipients or for assets to be left in trust for their benefit, as appropriate. If the recipients are relatively young or immature, the Will typically provides for a Trustee. Alternatively, for beneficiaries under the age of twenty-five, the Will can name a custodian for an account set up in the child's name. There are various considerations and alternatives in structuring these gifts, depending on the circumstances and objectives of the donor and the recipients, and the discussion of gifts to descendants in the preceding section pertains equally to gifts to other family members and/or friends.

a. Gifts to Parents, Siblings & Others. Sometimes an individual wants to leave his or her property to parents or siblings or a close friend for whom the individual cares to show love and regard but the intended beneficiary may not actually *need* the gift. If the beneficiary may not need the funds and/or such a gift would subject the property to estate taxes when the recipient dies, a couple of alternatives should be considered.

i. Such a gift can allow the intended beneficiary to *deflect* the amount gifted (or a portion thereof) to the intended beneficiary's children (or an appropriate trust for them) if the beneficiary doesn't need the funds. If the Will provides for such a possibility and the declination and deflection takes the form of a "qualified disclaimer", a deflection within a limited time following the donor's death won't constitute a taxable gift by the original intended recipient. Such a provision is especially attractive when an individual wants to leave assets to parents who may be elderly and/or comfortable and the individual's siblings are the alternative beneficiaries, and the individual is confident that the parents will reach an appropriate decision. Similarly, if the Will provides a gift to siblings or cousins or even friends who may or may not need the funds, it should be structured to permit recipient(s) to disclaim assets to their own children (or trusts for their children) below.

ii. An appropriately designed trust gift may make more sense than an outright gift. To the extent appropriate and desired, an individual's Will can establish a trust for the intended beneficiary that provides for the assets to be (1) controlled by the beneficiary, (2) available to the beneficiary (to the extent desired), and (3) subject to the beneficiary's power of disposition during life or at death (to the extent desired), but (a) not subject to claims by the beneficiary's spouse in the event of a divorce, (b) not subject to claims by the beneficiary's creditors, and (c) not subject to estate taxes when the beneficiary dies. Obviously, even when a trust is not required, a trust gift often makes far more sense than an outright gift.

b. Educational Trusts for Nephews & Nieces or Others. Sometimes a gift is earmarked for the education of nephews and nieces or others. The design of such a trust is limited only by the donor's imagination and can provide a number of incentives (or disincentives) to encourage pursuant of any education. The trust might provide for funds to be made *only* for the education of the beneficiary, with a "use it or lose it" structure that provides for the funds to go to the beneficiary's parents (or even to charity) if the beneficiary doesn't use them for education purposes prior to a certain age. Alternatively, the trust might provide a "graduation bonus", or distributions conditioned on the beneficiary's completion of the stipulated education.

PROVISIONS FOR CHARITY

If an individual wants to make charitable bequests, the Will may provide for *outright* gifts to one or more charities or for assets to be left in trust for charitable purposes.[7] Care should be taken to identify the charity properly, and the individual should consider whether he or she wishes to stipulate the purpose for which the bequest should be used.

[7] For a detailed discussion of charitable gifting strategies during life and at death, see the separate S&Z Monographs entitled ***"CHARITABLE GIVING: Making a Difference", "CHARITABLE REMAINDER TRUSTS: Doing Well while Doing Good", "CONSERVATION EASEMENTS: Preserving your Land for Posterity", "PLANNING PHILANTHROPY: Establishing a Private Foundation or Supporting Organization" and "CHARITABLE ESTATE PLANNING: Leaving a Legacy".***

a. Consider *Lifetime* Gifts. If the individual's resources are adequate, he or she should consider making gifts during his or her lifetime rather than by Will. *Lifetime* gifts save income taxes (in addition to saving estate taxes) while testamentary transfers save only estate taxes. In addition, the donor can observe (and help guide) the charity's use of the gifted funds, often receiving substantial personal satisfaction from doing the good deed during the donor's lifetime.[8]

b. Retirement Plan Dollars & Annuities. Assets such as installment sale contracts, qualified retirement plans or IRA balances and deferred annuity contracts that have built-in taxable income are referred to as "income in respect of a decedent" or "IRD", and *don't* receive a stepped-up basis when the owner dies. Such assets typically are worth more to a charitable beneficiary than to a family member, making them particularly good assets for charitable gifting. This is because a family member who receives such assets must pay income taxes on every dollar withdrawn. If a beneficiary is in the 35% tax bracket, he or she will net only $.65 on every dollar received. On the other hand, if a charity is designated as beneficiary to receive such assets, 100% of the value in the account inures to the charitable beneficiary since a charity is exempt from income tax. For this reason, individuals planning to leave part of their estates to family members or friends and part to charity should consider (1) leaving assets eligible for a basis stepup to family and friends, and (2) leaving IRD assets to charitable beneficiaries.

c. Conservation & Development Easements: Preserving Land for Posterity. If the individual owns real estate with special environmental value such as open space or wildlife habitat or extraordinarily scenic land adjacent to a public highway can provide for preservation of such special attributes and also obtain a charitable income tax deduction and estate tax savings by imposing a "conservation easement" designed to limit future development of such property.[9]

d. Charitable Remainder Trusts. If an individual wants to make a significant charitable gift but also wants to provide for a loved one, he or she can establish a "charitable remainder trust" to provide an income stream to the noncharitable beneficiary

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[8] See the S&Z Monograph entitled ***"CHARITABLE ESTATE PLANNING: Leaving a Legacy".***
[9] See the S&Z Monograph entitled ***"CONSERVATION EASEMENTS: Preserving your Land for Posterity".***

for life and provides for the underlying assets (i.e, the "remainder interest") to pass to a designated charity when the income beneficiary dies.[10]

NAMING A PERSONAL REPRESENTATIVE OR TRUSTEE

A function of an individual's Last Will & Testament or Living Trust as important as any other is to name the Personal Representative(s) of the individual's estate and/or successor Trustee(s). The Personal Representative is responsible for taking charge of the deceased individual's assets and affairs, managing and preserving asset values, paying taxes, debts or other claims, coordinating with financial advisors, attorneys and accountants as required, and carrying out the deceased individual's plan of disposition.

The most appropriate choice for Personal Representative will vary depending on an individual's circumstances and objectives. The most typical representatives are adult parents or siblings, adult children, close friends or business associates, other relatives, or institutional Trustees such as a Banks or Trust Companies. If an individual is designated, he or she must be competent, trustworthy and conscientious. He or she needs to be able to make time as required, and to work well with the deceased individual's legal, financial and accounting advisors. Ultimately, the Personal Representative doesn't have to know it all or do all of the work, but he or she should be the kind of person who will seek good professional advice when appropriate and who is capable of making good decisions.

Sometimes an individual will name multiple individuals (e.g. 2 or 3 individuals) as Co-Personal Representatives or Co-Trustees. Such a team may be less efficient but can make sense if the individuals can get along and work together effectively. Sometimes Co-Personal Representatives or Co-Trustees are named to tap different expertise (i.e., one individual may be the "financial guy" and the other a more intimate acquaintance with affected family members.) Other times, Co-Personal Representatives or Co-Trustees are named to build in a check and balance mechanism since multiple fiduciaries will be supervising the estate and will be accountable to each other. Other times, Co-Personal Representatives are named so that various affected beneficiaries have an equal voice in management and decision-making and don't feel excluded.

[10] See the S&Z Monograph entitled ***"CHARITABLE REMAINDER TRUSTS: Doing Well while Doing Good".***

If an individual is unsure who to name as Personal Representative or Trustee under the circumstances, it may make sense to name a professional fiduciary such as a Bank or Trust Company. The role of Personal Representative or Trustee is too important to entrust to an individual with dubious qualifications or only tenuous connections to the decedent. In such circumstances, using an institutional trustee or a professional Personal Representative may be the most sensible approach.

REVIEW & COORDINATE ASSET TITLING

While an individual's Will generally controls the disposition of his or her property at death, not all assets are *subject to* an individual's Will. Once an appropriate Will is signed, it is important to review the ownership and titling of all significant assets to ensure that they pass according to the plan.

Most of a decedent's property is controlled by the decedent's Will. However, upon the death of an individual, assets owned with other person(s) in "*joint tenancy with right of survivorship*" (JTROS) pass automatically to the surviving owner(s) by right of survivorship regardless of the provisions in the decedent's Will. In our experience, it is generally unwise for a single individual to hold assets in joint tenancy with right of survivorship with other people, including significant others or adult children, since such arrangements override provisions in the individual's Will and often give rise to disputes.

Such a problem arises most commonly when a single individual transfers assets into joint ownership with an adult child or another individual intending only to enable the other individual to help pay bills and/or manage assets. Joint ownership in such circumstances creates three significant risks: (1) the other joint tenant can legally withdraw funds from the owner's account unilaterally without the owner's knowledge or consent; (2) the other joint tenant will automatically inherit the property when the owner dies regardless of the provisions in the owner's Will, which may give rise to disputes among the heirs over whether this result was foreseen and intended; and (3) the assets are exposed to potential claims by creditors of the other owner(s). A safer and more appropriate approach is to give the individual a Durable Power of Attorney or mere signing authority over the account used to pay bills.

Review & Coordinate Beneficiary Designations

Similar considerations apply to life insurance, annuities and retirement plan accounts that are controlled by beneficiary designations. When an individual dies, such assets generally are paid to the designated beneficiary(ies) and are *not* controlled by provisions of the owner's Last Will & Testament.

With life insurance, it is simply a matter of review and coordination of the controlling beneficiary designations. With annuity contracts, there are also income tax implications for the beneficiaries that should be taken into consideration because the beneficiaries are treated as receiving taxable "income in respect of a decedent" when they receive payments.

Planning for qualified retirement plan assets and IRAs is more complicated because there are a number of very technical and often conflicting rules that make it hard to generalize regarding the optimal strategy. Appropriate planning depends on a person's particular situation and objectives and involves the review of distribution options available under the Plan documents and the law during the participant's lifetime and after his or her death. Ultimately, the most appropriate beneficiary designations require consideration and balancing of the beneficiary's need for funds, the beneficiary's ability to manage the funds, and complex income tax and estate tax considerations. Sometimes, it is also desirable and important to build-in an *alternate* beneficiary designation giving a beneficiary post-mortem flexibility to trigger with a qualified disclaimer.

Supplemental Medical & Long-term Care Insurance

As part of the estate planning process, individuals should evaluate their need for supplemental medical insurance or long-term care insurance. Even if available resources are more than adequate to cover such costs, some individuals find insurance attractive to avoid the risk that if a need arises, such costs will consume the assets they hope to leave to loved ones.

In the not-too-distant past individuals who anticipated (or feared) that the high costs of nursing home care might consume assets they hoped to leave to their children, would give their property to their children prior to admittance in the hopes of becoming eligible for Medicaid assistance. Many individuals disapprove of such artificial impoverishment attempts to qualify for public assistance. Others are dissuaded from such tactics by the real or imagined fear that care to Medicaid patients is inferior. In any event, changes to Medicaid rules in recent years have significantly restricted such strategies. However, in some limited circumstances, a few planning options remain for individuals who are willing to transfer their remaining property to their children well ahead of time.

ADVANCED ESTATE PLANNING

Once an individual has the basic foundational estate planning arrangements in place, the "second phase" of estate planning entails strategies to address specific concerns or achieve particular objectives. An individual looking at a significant estate tax liability may consider gifting and leveraged gifting strategies to reduce estate taxes.[11] An individual with a substantial retirement plan account balance may plan to facilitate continued income tax deferral on retirement plan assets by their children and grandchildren.[12] Individuals engaged in a risky occupation or who are nervous about potential liability or creditors' claims may explore asset protection strategies that minimize such exposure.[13] Individuals with closely-held business interests may plan for business succession to ensure business survival and/or a buy-sell agreement to provide a liquidity option.[14] Finally, for individuals committed to philanthropy, charitable planning strategies are important.[15] The paragraphs that follow are intended to provide an overview of each of these important areas of concern.

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[11] See S&Z Monograph entitled ***"GIFTING & LEVERAGED GIFTING: How to Maximize Estate Tax Savings".***
[12] See S&Z Monograph entitled ***"THE ETERNAL IRA: Leaving your Retirement Account to your Heirs".***
[13] See S&Z Monograph entitled ***"ASSET PROTECTION PLANNING: Hedging your Bets".***
[14] See S&Z Monographs entitled ***"BUY-SELL AGREEMENTS: Cornerstone of your Business Plan", "FAMILY BUSINESS SUCCESSION PLANNING: Keeping a Business in the Family" and "QUALIFYING FOR THE QFOBI DEDUCTION: ESTATE TAX Relief for Closely-Held Business Owners".***

PLANNING TO REDUCE OR MITIGATE ESTATE TAXES

When an individual dies, the value of his or her property (everything he or she owns or controls, including life insurance, retirement plan assets and even some assets that have been given away) in excess of $5.43 Million is subject to federal estate tax. Each of us has a *lifetime exemption* from estate taxes of $5.43 Million in 2015[16], and value greater than that amount will be subject to a federal estate tax at a rate of 40%, and a state estate tax at rates ranging from 10% to 20%. This means that an individual may leave up to $5.43 Million to anyone in the world, during life or at death, free of federal and state estate tax liability. However, if an individual's property is worth more than this amount, federal and state estate tax will be due when he or she dies unless action is taken to minimize estate taxes. The good news, however, is that the estate tax is often referred to as a "voluntary tax" because available planning strategies can dramatically reduce estate tax liability in the end.

For individuals with taxable estates (i.e., greater than the $5.43 Million lifetime exemption), there are various planning options. Every unmarried individual's estate is taxable in the end except to the extent property in excess of $5.43 Million is left to charity. Therefore, unless an individual wants to leave his or her property to charity[17], planning is necessary to avoid the tax. Such planning typically revolves around some combination of: (1) *gifting and leveraged gifting strategies*[18] to reduce the individual's taxable estate by taking advantage of and leveraging gift tax exemptions as early as possible during the individual's lifetime and at death, (2) *strategies to fragment ownership of assets*[19] to qualify for valuation discounts that minimize the value taxable in the end, and (3) *strategies to mitigate the impact of estate taxes* through liquidity planning, often involving life insurance

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[15] See S&Z Monograph entitled ***"CHARITABLE ESTATE PLANNING: Leaving a Legacy".***

[16] The federal gift tax lifetime exemption amount is $5.43 Million, the same amount as the federal estate tax exemption amount (although lifetime gifts in excess of the annual exclusion amount reduce the federal estate tax exemption amount). Washington State does not have a gift tax. The Washington state estate tax exemption amount is $2,054,000 Million in 2015. Both the federal exemption amount and the Washington estate tax exemption amount are scheduled to increase with inflation.

[17] See S&Z Monograph entitled ***"CHARITABLE ESTATE PLANNING: Leaving a Legacy".***

[18] See S&Z Monograph entitled ***"GIFTING & LEVERAGED GIFTING: How to Maximize Estate Tax Savings".***

[19] See separate S&Z Monographs entitled ***"GIFTING & LEVERAGED GIFTING: How to Maximize Estate Tax Savings"*** and ***"FAMILY PARTNERSHIPS: Everything you Need to Know".***

purchased through a life insurance trust to *pay* estate taxes that cannot be avoided[20]. An overview of these strategies is provided below.

Gifting & Leveraged Gifting Strategies to Save Estate Taxes

For those individuals concerned with the bottom line of avoiding transfer taxes, gifting is the answer. However, the advantages of making gifts are only truly realized by those who understand the intricacies of the transfer tax system and utilize it to maximize the allowable benefits. At the core of almost all tax-motivated gifting is the ability to transfer up to $14,000 per recipient, per year, without incurring a single dollar in gift taxes. Such gifts are known as "annual exclusion gifts".

Many people would like to make gifts to a minor, either strictly for educational purposes, or for future support. However, as a general rule, it is always unwise to make direct gifts to a minor.[21] Therefore, some form of ownership is necessary to hold the gift for the minor during his or her formative years. Alternative gifting arrangements exist which allow the donor to appoint a Custodian or Trustee to control the gifted property. This form of gifting guards against the minor squandering the gifted property during adolescence. Qualifying gifts to minors to pass free from the federal gift tax is the fundamental goal of such a gifting program.

A single person may wish to establish and continue an annual program of gifting to reduce his or her estate. By utilizing the annual exclusion, the individual is taking an affirmative step toward reducing his or her estate without adverse tax consequences. However, by leveraging the annual exclusion gift, a person can make superior use of the benefits of gifting.[22] In almost all cases of single people with taxable estates, lifetime gifts using annual exclusions nearly always make sense.

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[20] See separate S&Z Monographs entitled ***"LIFE INSURANCE: The Simplest Solution for Estate Taxes", "LIFE INSURANCE: Part of a Diversified Estate Plan",*** and ***"LIFE INSURANCE TRUSTS: Getting the Most from your Life Insurance".***

[21] The diverse and useful methods of making gifts to minors is discussed in the Smith & Zuccarini, P.S. Monograph "Gifting to Minors – A Comprehensive Look at Your Options".

[22] The benefits and methods of leveraging gifts is discussed in greater detail in the Smith & Zuccarini, P.S. Monograph entitled "Gifting and Leveraged Gifting – For Estate Tax Savings".

Transfer Life Insurance to an Irrevocable Trust

In addition, because proceeds of insurance policies owned and controlled by the insured are included in his or her taxable estate for federal estate tax purposes, individuals with significant assets and/or life insurance are well advised to consider establishing an Irrevocable Life Insurance Trust to own their life insurance to avoid estate taxes otherwise due thereon. Since single people do not have the option of deferring estate taxes by way of the marital deduction, placing life insurance in an irrevocable trust can be a significant way to provide liquidity necessary to pay estate taxes.

Single people who own or plan to acquire a significant amount of life insurance should consider establishing an Irrevocable Life Insurance Trust (an ILIT) to own their life insurance policies in order to avoid estate taxes otherwise due on their life insurance proceeds when they die.[23] The simplicity and effectiveness of the ILIT technique makes it one of the most popular estate planning strategies today. The ILIT provides for the avoidance of estate tax on life insurance proceeds, some degree of control over the ultimate use of the insurance proceeds and the ability to leverage various estate and gift tax exemptions. Typically, a Life Insurance Trust is established by the insured. The Trust is irrevocable, and the Trustee should be technically *independent* (i.e. most individuals name a sibling or child unless a professional trustee is preferred).

The insured transfers to the Trustee all ownership rights over existing life insurance policies, or cash to be used to purchase new life insurance policies, and makes additional annual transfers to the Trustee to be used to pay annual premiums. When the insured dies, the proceeds are paid to the Trustee, and the Trust Agreement is properly drafted, the proceeds will be excluded from the insured's taxable estate.

Ultimately, an Irrevocable Life Insurance Trust may be used to preserve *existing* life insurance policies from erosion by estate taxes, or may be used to purchase a *new* life insurance policy outside the insured's taxable estate. In either event, because the federal estate tax rate is 40%, the potential savings may be substantial. And if the Life Insurance Trust is designed as a "Dynasty Trust" to benefit more than one succeeding generation of the descendants with appropriate generation-skipping transfer tax provisions, the combined estate tax savings can be truly enormous.

Giving Assets Away without Giving Up Control & Benefit

While gifting may be the easiest way to decrease an individual's estate, many people are not ready to relinquish control over the gifted items. Retention of control is even more important for the person who owns a single asset, such as a home or closely held business, which constitutes the bulk of his or her estate. Fortunately, there are a few estate planning techniques that allow a person to remove property from his or her estate while still retaining control over the relinquished asset.

One such technique is the qualified personal residence trust (QPRT). A QPRT allows a person to pass on the family home to the next generation while retaining the use and enjoyment of the home during his or her lifetime.[24] By utilizing a QPRT, the fair market value of the property as well as its entire future appreciation is removed from the donor's estate by making a gift today of a future interest in the property. The gift tax incurred by the transfer is merely a fraction of the estate tax which would have otherwise been incurred had the house (and its future appreciation) been left in the donor's estate.

Fragmenting Ownership to Reduce Taxable Values

A method of transferring value and retaining control is to gift units in a family limited partnership.[25] Such a technique allows a person to retain the right to vote in a company and to gift away the non-voting ownership interest. As limited partners, the recipients own their proportional share of income and capital of the partnership, but they have no right to participate in the management or control decisions of the partnership.

[23] The potential benefits of the Irrevocable Life Insurance Trust technique, and the mechanics for establishing and implementing an ILIT, are described in detail in a separate Smith & Zuccarini, P.S. Monograph entitled "Irrevocable Life Insurance Trusts- Getting the most from your Life Insurance."
[24] The substantial tax savings as well as the intricate qualifications for using a QPRT are discussed in detail in the Smith & Zuccarini, P.S. Monograph "The House Trust – An Incredible Estate Planning Technique".
[25] The unique use of a business entity to transfer wealth out of an estate is discussed in detail in the Smith & Zuccarini, P.S. Monograph "Family Partnerships – Everything You Need to Know".

Additionally, gifts of non-voting units can be discounted due to a lack of marketability. The end result is a "stuffing" of value into an annual exclusion gift.

Strategies to Mitigate the Impact of Estate Taxes

Many individuals with substantial taxable estates are reluctant to make lifetime gifts on the scale necessary to reduce or eliminate anticipated estate taxes at the present time. Life insurance addresses a short term need for a single person to provide for his or her children in the event of an early death. Single life policies are indispensable tools for planning the estate of a single person. Such life insurance provides a hedging function without counterpart in other investing.

Review of the sufficiency of a person's existing life insurance coverage should be part of the estate planning process. Since Smith & Zuccarini, P.S. is *not* in the business of *selling* life insurance, we are uniquely situated to provide objective advice concerning the potential benefits of life insurance in estate planning and appropriate coverage amounts, and we are experienced in planning with life insurance.

Life Insurance, like qualified retirement plan assets, comprises a significant part of many individuals' net wealth and is another "nonprobate asset" that typically passes outside the individual's probate estate. Typically, when an individual insured dies, the proceeds of life insurance policies on his or her life are paid to the designated beneficiary, and unless the individual's estate is designated as the beneficiary, the provisions of his or her Will are irrelevant. Consequently, careful consideration should be given to where the funds should be paid, who should control the ultimate disposition of the insurance proceeds, and similar issues.

Charitable Estate Planning Strategies

As noted above, estate taxes are eliminated to the extent assets are left to charity when an individual dies. For individuals who want to leave all or a substantial portion of their assets to charity, charitable gifts eliminate estate tax concerns altogether. However, even for individuals who have noncharitable beneficiaries uppermost in mind, so-called "split interest" charitable gifting strategies such as charitable remainder and charitable lead trusts can be used to accomplish noncharitable objectives more tax-efficiently.[26]

ASSET PROTECTION PLANNING

Along with disposing of assets and ensuring final arrangements, estate planning can serve as a shield to ward off others from one's hard earned assets. By placing assets in a personal asset protection trust, a person can insulate assets from creditors for the benefit of another. Along those same lines, a limited liability entity can be established in order to protect an individual's assets from the creditors of a partnership or company.

The personal asset protection trust is a great way to gift assets to a successful child or grandchild, and still insure that the assets will not be subject to creditors. The beneficiary can control and access the trust and can even be named the Trustee. Such a trust can also be used to provide for a beneficiary who is financially overextended or for whom a divorce is pending.[27]

The limited liability company also provides insulation from personal liability for claims arising from the underlying property. This means that the individual will not be personally liable for the debts and obligations of the business beyond his or her financial interest in the business. In other words, it provides asset protection for personal items.

BUSINESS SUCCESSION PLANNING

When an individual owns a closely-held business or a significant interest in a business, special consideration must be given to such interest as part of estate planning process. Planning aims to ensure the survival of the business, and realization of its value by the individual's surviving family members or other beneficiaries.

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[26] The many uses of a Charitable Remainder Trust and the intricate criterion for qualifying are discussed in a separate Smith & Zuccarini, P.S. Monograph entitled "Charitable Remainder Trusts – Doing Well While Doing Good".

[27] The many uses of the Personal Asset Protection Trust are described in detail in a separate Smith & Zuccarini, P.S. Monograph entitled ***"ASSET PROTECTION STRATEGIES: Hedging Your Bets"***

Business succession planning may emphasize the tax-wise sale or gifting of ownership to family members, or seek to facilitate the orderly sale of the business to co-owners, key employees, or others. Consideration also should be given to the individual's ability to qualify for special estate tax relief provisions available to owners of closely-held businesses, and to the need for both key-man life insurance for the Company and personal life insurance to assist the owner in paying estate taxes without a forced sale of the Company or other assets.

SUGGESTED APPROACH TO ESTATE PLANNING

We recommend that people tackle their estate planning in two steps: The first phase consists of implementing the basic "foundational" estate planning arrangements that everyone needs including an appropriate Will or Living Trust to carry out the individual's desires and provide appropriately for loved ones, as well as a Durable Power of Attorney for Financial Matters and Health Care Decisions, and a Health Care Directive (also known as a "Living Will"). In addition, the precise form of ownership and titling of each significant asset needs to be reviewed to ensure that it is appropriately coordinated with the provisions of the Will or Living Trust. Finally, life insurance, annuity contracts, and retirement plans or IRAs need to be reviewed and the beneficiary designations and other elections carefully coordinated with provisions of the individual's Will or Living Trust.

The second phase of estate planning consists of advanced planning to address specific objectives or concerns, including (1) strategies to reduce the burden of anticipated estate taxes, (2) strategies to maximize income tax deferral related to a significant retirement plan account, (3) business succession planning, (4) asset protection planning, and (5) philanthropic estate planning.[28] Depending on a person's particular situation and objectives, the second phase may be the most important part of their personal planning, or it may be entirely unnecessary.

Attorneys at Smith & Zuccarini, P.S. have assisted single people with their estate planning over more than two decades and are thoroughly familiar with estate planning

[28] Smith & Zuccarini, P.S. has prepared separate Monograph dealing with each of these topics that are available upon request.

strategies and techniques. We are happy to meet with you to review your particular circumstances, and help you determine the most appropriate planning strategies for *you*.

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