Estate Planning

Introduction

Estate planning is more than the process of making sure that your property will go to those you choose. It also involves continuing to control your property while you are alive, providing for the care of you and your family if you are disabled, controlling the way your property passes, and saving every possible tax dollar, professional fee, and court cost. Whether your estate is large or small, you have the right to decide what will happen to it upon your death. In addition to deciding who should receive your property, your estate plan must consider the value of your estate, the probate process, provisions for your care during a period of illness or incapacity, methods to transfer your property, techniques to reduce or eliminate estate taxes, and the choice of the persons you want to supervise the transfer of your property or care for minor children and incapacitated persons.

Working together as a team produces the best plan

The lawyer preparing your estate plan must have a complete picture of your personal situation, including your assets and income sources, to develop the best plan for you. That means the lawyer must not only work closely with you, but also must coordinate with your accountant, insurance agents, and investment advisors. A failure to work with these other professionals involved in your financial affairs may result in unnecessary duplication of efforts and could bring unforseen results that defeat the purposes of the plan.

Value of your taxable estate

Before you can decide how best to pass the assets which make up your estate, you first need to know what actually comprises the property of your estate. Your taxable estate will include everything you own at the time you die: house, furniture, savings and checking accounts, securities, insurance policies, retirement accounts, and annuities. The actual value of your taxable estate can only be computed after you die. However, to do a good estate plan, you and your lawyer must estimate the current value of your estate. This estimate is needed to anticipate and plan for the cost of probate and estate taxes due when you die and to consider techniques to minimize these costs.

Calculating the value of your current estate is not difficult. First, you prepare a written list of what you own and put a value on each item. The full value of everything you own by yourself must be included. Part of the property you own jointly with other persons will also be included. If you own the property as joint tenancy with right of survivorship or tenancy by the entirety with your spouse, one-half of the property's value must be included in your estate. If you own property in joint tenancy with right of survivorship with your children and they did not help purchase the property, all of the value of that property must be included in your estate. When you own property as a tenant in common, the amount included in your estate will depend on your fraction or percentage of ownership. For example, if you are a one-third owner as a tenant in common, your estate will include one-third of the total value of the property. The amount of the death proceeds of any insurance policy which you personally own and name you as the insured life (i.e., will pay out on your death) must be included on your list. Your retirement and annuity account balances must also be included. If your retirement plan has a survivor benefit rather than an account balance, an estimate of the survivor's benefit value must be included. For a discussion of retirement planning, please go the Retirement Planning topic on our Web site. You must also include the total value of any trusts for which you hold a power to appoint the trust assets to yourself and any trusts in which your spouse gave you a right to income in return for an estate tax or gift tax marital deduction (known as a qualified terminable interest trust or QTIP). The total value and type of all the property described on your list will constitute your current estate and will be used by your attorney and other advisors to create an appropriate estate plan.

Calculating your taxable estate at your death will constitute the same basic process. The total value of all the property you own at your death will be calculated to determine your "gross estate." After the value of your gross estate has been determined, you will subtract from it the deductions provided to you under the Internal Revenue Code. Such deductions will include estimates of funeral costs, outstanding debts, and administrative expenses of settling your estate. If you are married, you will also be allowed a marital deduction for everything you leave to your spouse if he or she is a United States citizen. You are also permitted an unlimited charitable deduction for gifts to charities occurring at your death. After you subtract these deductions from your "gross estate," you will be left with your "taxable estate."

Gift and Estate Tax

The actual amount of estate tax your estate will pay is based on your "taxable estate" as adjusted for previous taxable gifts and gift and estate tax credits. Under current law, every person who is a U.S. citizen or a permanent resident may gift or pass by inheritance to others up to a certain amount of property without paying any federal gift or estate taxes. This amount is called the applicable exclusion amount because it is based on the amount protected by a credit against gift and estate taxes. The credit applies regardless of the identity, relationship, or citizenship of the persons or entities receiving your estate. If the value of your tentative taxable estate at your death exceeds your remaining applicable exclusion amount, estate tax may be due.

At the end of 2012, the 2012 Taxpayer Relief Act was adopted by Congress. Among other things, this Act made permanent an applicable exclusion amount for each U.S. citizen or permanent resident of $5,000,000, as adjusted for inflation. The "applicable exclusion" amount for 2017 is $5,490,000. Additionally, the 2012 Taxpayer Relief Act made permanent a new exclusion tool known as "portability." Portability is the right of a surviving spouse to elect to carry over and use the remaining applicable exclusion of his or her deceased spouse at the death of the surviving spouse. So, for 2017, a surviving spouse making the portability election could potentially have a total applicable exclusion amount of twice the individual applicable exclusion, or \$10,980,000. In order to make the election, the surviving spouse, personal representative of the deceased spouse's estate, or trustee of the deceased spouse's trust must make the election on a timely filed IRS Form 706, known as the Estate (and Generation-Skipping Transfer) Tax Return. To be timely filed, the Form 706 must be submitted to the IRS within 9 months of the deceased spouse's date of death, or within 15 months of the deceased spouse's date of death if a request for extension of the filing period is filed. A typical Form 706 requires the production of very detailed and accurate information regarding a deceased person's assets. However, the new Form 706 provides a much lower standard for reporting the value of a deceased person's assets if the only reason for the filing of the Form 706 is to make the portability election. If a portability election is made, the surviving spouse's applicable exclusion amount will include both the surviving spouse's exemption plus the amount of the deceased spouse's unused exclusion amount for which the portability election was made.

The estate tax due on your estate will be calculated based on your taxable estate after adding to the taxable estate any taxable gifts you made after 1976, and subtracting any gift tax you paid during your lifetime. Your total applicable exclusion amount (including any applicable deceased spouse unused exclusion) will be subtracted from this total to determine the amount of your estate subject to estate tax. The amount subject to estate tax will be taxed at a rate of 40%. Since your taxable estate includes everything you owned at death, including the assets that will be used to pay estate taxes, the estate tax is a tax-inclusive tax.

Most married couples can avoid paying estate tax when the first person dies by leaving everything to their surviving spouse. The unlimited estate tax marital deduction will protect the property left to the surviving spouse and avoid estate tax. Congress has made this technique even more effective by adopting the portability election, mentioned above. The portability election, in effect, allows the surviving spouse's estate to take a double exclusion equal to twice the applicable exclusion amount. However, if your combined assets exceed two times the applicable exclusion amount, leaving everything to your spouse will only defer the estate tax until the second death. As an example, we will look at the case of a married couple, Sam and Irene, who acquired property worth \$12,000,000 during their lifetimes. If they own all of their property jointly or have wills providing all the property of the first to die goes to the survivor, there will be no estate tax upon the first death, but an estate tax of approximately \$408,000 will be due at the second death, assuming they both died in 2017 and we use the applicable combined exclusion amount of \$10,980,000. For purposes of illustration, we will assume Sam dies first and Irene dies shortly thereafter and there is no growth or shrinkage of their property between deaths:

If Sam owned \$6,000,000 and Irene owned \$6,000,000:

Sam's Estate Date of Death 5/1/2017

Gross Estate	\$6,000,000

Marital Deduction	$6,000,000
Taxable Estate	$0
Applicable Exclusion Amount	$5,490,000
Amount Taxed	$0
Tax (rate 40%)	$0
Amount of Exclusion left to Irene	$5,490,000

Now, Assume Irene dies three months later after inheriting $6,000,000 from Sam:

Irene's Estate Date of Death 8/1/2017

Gross Estate	$12,000,000
Taxable Estate	$12,000,000
Applicable Exclusion Amount ($5,490,000 carried over from Sam and $5,490,000 for Irene)	$10,980,000
Amount Taxed	$1,020,000
Tax (rate 40%)	$408,000
Amount left to Children	$11,592,000

If Sam and Irene owned $12,000,000 jointly, the result would be the same:

Sam's Estate Date of Death 5/1/2017

Gross Estate (½ of the jointly owned $12,000,000)	$6,000,000
Marital Deduction	$6,000,000
Taxable Estate	$0
Applicable Exclusion Amount	$5,490,000
Amount Taxed	$0
Tax (rate 40%)	$0
Amount of Exclusion Left to Irene	$5,490,000

Now, assume Irene dies one month later after inheriting $6,000,000 from Sam pursuant to their joint ownership.

Irene's Estate Date of Death 8/1/20147

Gross Estate	$12,000,000
Taxable Estate	$12,000,000
Applicable Exclusion Amount ($5,490,000 carried over from Sam and $5,490,000 for Irene)	$10,980,000
Amount Taxed	$1,020,000
Tax (rate 40%)	$408,000
Amount left to Children	$11,592,000

There are ways to avoid an estate tax upon the second death by removing property from a person's taxable estate. For further discussion of these techniques, please go to the Family Gifting, Insurance Trusts, and Charitable Gifts topics on our website. It is important to remember that a married couple owning together more than double the applicable exclusion amount will have an estate tax due upon the second death unless they use estate planning to avoid it.

Marital deduction and credit shelter planning for a married couple

Credit shelter planning is a strategy that can be used when a couple decides not to elect to use portability in order to carry over the exclusion amount of the first to die or just carries over part of the exclusion amount of the first to die. This decision may be applicable when a couple owns assets which are appreciating rapidly and they want to keep them out of the surviving spouse's estate, or when a couple doesn't want to file an IRS Form 706 estate tax return in order to make the portability election. Although the reporting requirements for a Form 706 that is being filed for the sole purpose of making the portability election are much less extensive , there will still be a cost to prepare and file the return. Your surviving spouse and his or her advisors would want to make the decision of whether or not to file the Form 706 after taking into account the costs and benefits of such action.

If a married couple's combined assets exceed the value of one person's applicable exclusion amount ($5,490,000 in 2017), and the portability election is not going to be made, it becomes necessary to engage in estate planning to avoid estate tax on the second death. The basic estate planning technique to avoid an estate tax on the second death is a will or trust with a two-share arrangement. This technique is commonly called "credit shelter" planning and is sometimes called the A - B trust arrangement. Whatever you call it, this technique will permit up to double the applicable exclusion amount to pass to children or other designated beneficiaries without payment of estate tax on either spouse's death.

To make credit shelter planning work, a mechanism must be in place to permit each spouse to use enough of his or her applicable exclusion amount upon death to avoid estate taxes on both deaths. This can be done through formula provisions, disclaimers, or a partial election of the estate tax marital deduction. The idea is to use some or all of the first-to-die's applicable exclusion amount to set aside property and protect it from estate tax on the second death. If a couple's combined assets are valued at two full applicable exclusion amounts or more ($10,980,000 or more in 2017), the amount set aside on the first death would have to be the first-to-die's full applicable exclusion amount ($5,490,000). If a couple's combined assets are worth less than $10,980,000, the amount set aside should be large enough to ensure the surviving spouse will not have property worth more than $5,490,000 when he or she dies.

This separation of ownership can be accomplished by having each spouse own assets separately, having assets separately owned by each person's revocable trust, or by having assets owned in a joint revocable trust. When trusts are used to divide ownership, the husband and wife can serve as co-trustees of the trusts and, for all practical purposes, they both will continue to participate in the management, investment, and other decision making for all family assets as they did before the division.

In an estate plan using credit shelter planning, the separate wills or revocable trusts of both the husband and wife, or the joint revocable trust will contain provisions that divide the property of the first-to-die or the joint trust property into two parts. The first part, which may be called the credit shelter share, credit shelter trust, bypass trust, or family trust, will be the amount protected by the applicable exclusion amount of the first-to-die. This amount can be distributed to a credit shelter or family trust for the benefit of the surviving spouse and the children, to a credit shelter trust solely for the benefit of the children, or directly to the children. This amount will not be subject to estate tax upon the second death, no matter how much it grows between deaths, because it will be forever protected by the applicable exclusion amount of the first-to-die. If there is any remaining amount of the first-to-die's property or joint trust property not protected by the first-to-die's applicable exclusion amount, that amount will be allocated to a marital share. The marital share could be distributed outright to the surviving spouse, distributed to his or her revocable trust, or distributed to a marital trust or survivor's trust for the benefit of the surviving spouse.

If the applicable exclusion amount of the first spouse is used for a credit shelter trust benefitting the surviving spouse and the children, the surviving spouse may have significant rights with respect to the property of the trust. He or she may be the trustee of the trust, receive all of the income from the trust, and withdraw trust property as needed for his or her health, education, support, and maintenance. The surviving spouse may also be permitted to withdraw up to $5,000 or 5% of the trust property annually for any reason and be permitted to appoint the property of the trust at his or her death among the couple's deserving children.

If the amount not protected by the first-to-die's applicable exclusion amount is held in a marital trust or survivor's trust for the benefit of the surviving spouse, the trust terms may be very broad or restrictive, depending on the family situation. If broad powers are desired, the surviving spouse may receive all the income from the trust and be permitted to withdraw principal for any reason. He or she may also appoint the trust property at death to anyone. If the family situation involves a second marriage and children exist from the first marriage, more restrictive terms may be desired. In that case, the surviving spouse may be limited to only receiving all the income from the trust and all assets will pass to the children of the first marriage when the surviving spouse dies.

Let's apply this credit shelter trust and marital trust concept to an example in which Sam and Irene have an estate worth $10,000,000. Instead of the ownership in our previous examples, Sam and Irene divided their $10,000,000 of assets into equal shares and created wills or revocable trusts with a credit shelter/marital trust arrangement or they transferred their jointly owned assets into a joint revocable trust with such an arrangement. We will assume Sam dies first.

Sam's Estate

Sam's Gross Estate	$5,000,000
Marital Deduction	$0
Taxable Estate	$5,000,000
Applicable Exclusion Amount Used (placed in a credit shelter trust for Irene and their children	$5,000,000
Amount taxed	$0
Amount of tax	$0
Irene still has $5,000,000 of her own assets, plus she has access to the assets in Sam's credit shelter trust, with some limitations. Plus, she could choose to elect portability to carry over Sam's remaining $490,000 applicable exclusion for use at her death.	

Irene's Estate

Gross Estate	$5,000,000
Marital Deduction (None is available since Sam died first	$0
Taxable Estate	$5,000,000
Irene's Applicable Exclusion Amount if no portability election is made	$5,490,000
Amount Taxed	$0
Amount of Tax	$0
Amount passed to children free of estate tax from Irene's estate and Sam's Credit Shelter trust combined	$10,000,000

Charitable deduction and credit shelter planning for a single person, widow, or widower

When a single person, widow, or widower owns property in excess of the applicable exclusion amount at his or her death, credit shelter planning can be used in combination with the unlimited charitable deduction to eliminate or reduce estate taxes. The widow or widower using this technique gives the applicable exclusion amount outright or in trust to his or her children or other relatives. The remainder of the estate then passes outright or in trust to charitable beneficiaries. If the bulk of the estate is a family farm, ranch, or business, the special value reductions permitted for such property can be combined with the credit shelter planning to distribute up to $6,430,000 to qualified relatives of the deceased widow or widower estate tax free.

Because of the lack of a marital deduction, estate planning for single, persons, widows, and widowers may need to include techniques to remove property from the person's estate before or after death. There are many techniques that can work very well to reduce or eliminate estate tax when the estate of a single person exceeds his or her applicable exclusion amount or the combined estates of a married couple exceed twice the applicable exclusion amount.

Gift Tax

As discussed above, after January 1, 2011, the estate and gift tax are once again unified as one system. The "applicable exclusion amount" for gift tax is $5,490,000. This means you may give away $5,490,000 during your life without paying any gift tax. The gift tax applicable exclusion amount is a lifetime gift tax exclusion amount and is in addition to the $14,000 per person per year gifts you may give as "annual exclusion gifts." Lifetime gifts made with the gift tax applicable exclusion amount will reduce the remaining available estate tax applicable exclusion amount.

Basics of the Generation Skipping Transfer Tax

The generation-skipping transfer tax is a flat tax imposed at the highest estate tax rate, currently 40%. It is imposed when property passes to beneficiaries who are two or more generations younger than the giver's generation. For example, if a giver were to establish a trust for a child for life with the remainder on the death of the child passing to the grandchildren, a generation-skipping transfer tax could be imposed on the property in the trust at the child's death. If the beneficiary of the gift is not a direct family member, he or she is considered to be two or more generations younger than the giver if there is at least 37.5 years difference between their ages.

The generation-skipping transfer tax can become very burdensome when the value of the transfer is greater than the annual gift tax exclusion amount (currently $14,000). Consider an interest in property worth $500,000 which is transferred by a grandparent to a grandchild, or to a trust for a grandchild, during the grandparent's life. In this situation, the transfer will be subject to two taxes – a gift or estate tax and the generation-skipping transfer tax.

The 2012 Taxpayer Relief Act not only made the estate and gift tax exemption amount permanent at $5,000,000 (as adjusted for inflation), it also set the exemption amount from generation-skipping transfer tax at $5,000,000 (as adjusted for inflation). Therefore, the exemption amount for the estate and gift tax is the same as the exemption amount for the generation-skipping transfer tax. In 2017, there is a $5,490,000 exemption from the generation-skipping transfer tax available to each person without regard to whom or how the generation-skipping transfer are made. Therefore, a person can establish a trust for their children for life, then for their grandchildren for life, with a remainder to great grandchildren and fund it with up to $5,490,000, either during life or upon death. The trust would be exempt from the generation-skipping transfer tax for the duration of the trust and would avoid estate tax at the death of the child and at the death of the grandchild. The transfer into the trust may be subject to either federal gift or estate tax, depending upon whether it was made during life or at death, taking into account whether the grantor has any remaining unused gift and estate tax exclusion to be applied toward the gift to the trust.

If the assets of a single person will not exceed $5,490,000 at his or her death, the assets will be covered by the generation-skipping transfer tax exemption to the extent that the person has not used the exemption during life. Additionally, if the total assets of a married couple will be worth between $5,490,000 and $10,980,000 at the death of the surviving spouse, the assets will be exempt from the generation-skipping transfer tax only if the couple's estate planning instruments are drafted with this tax in mind, and the property is titled correctly.

The portability rules do not provide a means to transfer the generation-skipping exemption between spouses; therefore, it is important to evaluate how and if generation-skipping transfers should occur. It might be in the best interest of the spouses to transfer adequate assets into each spouse's individual name (or in his or her revocable trust) in order to use the exemption, regardless of the order of death. Alternatively, if the couple is using a joint trust estate plan, upon the death of the first spouse, the surviving spouse may elect to create a trust for the benefit of the couple's children and grandchildren which uses the deceased spouse's generation-skipping transfer tax exemption at his or her death. Additionally, it might be desirable to just leave more property to children and not skip directly to the grandchildren if part of the exemption has already been used.

A direct gift to a grandchild that qualifies for the $14,000 annual gift tax exclusion or for the medical or education tuition gift exclusion, will also avoid generation-skipping transfer tax.

Basis of Property Acquired from a Decedent

Basis, which is generally equivalent to the cost of an asset, determines the amount of taxable gain on the subsequent sale or disposition of the asset. The basis of property acquired from a decedent is stepped-up or down to the value of the property on the date of death or at an alternate valuation date six months after death. However, if property is given to a decedent within one year of death and is inherited by the giver or the giver's spouse, the basis of the property is not stepped up.

Probate

Estate Planning must consider the impact of two types of probate. Both types of probate are avoidable with proper estate planning. The first type is living probate. Living probate does not require a death. Living probate occurs when a minor or incompetent person owns or receives property. Living probate may occur when you make an outright gift of property to a minor child or grandchild. It may also be required when a person who owns property by himself or jointly becomes incompetent to handle his own affairs. Under the law, when a minor or incompetent owns property, a conservator must be appointed by the probate court to protect the interests of the minor or incompetent. If two persons own real property jointly and one becomes incompetent, a conservator will also have to be appointed to act for the incompetent before the property can be sold or transferred.

The conservatorship process is a court proceeding requiring a lawyer, court costs, conservator fees, and the continuing supervision of the probate court. The property of the minor or incompetent cannot be sold or otherwise transferred without court approval. The court-appointed conservator must account to the court periodically for the assets of the minor or incompetent. Sometimes, living probate can be more expensive than death probate because court supervision continues until the minor reaches legal age or the incompetent dies or regains competency.

The second type of probate is death probate. Death probate is required if you die with or without a Will. Probate will also be required on the second death of a married couple when property passes by joint ownership or beneficiary designation on the first death. Probate is a legal process of ensuring your debts and expenses are paid and the property you own at death is distributed as provided in your Will or as provided by the law. If you have a Will, the personal representative named in the Will is responsible for taking care of probate. If you die without a Will, the court will appoint an administrator to handle the probate process.

In Wyoming, formal probate is required if a person dies owning more than $200,000 in property which is subject to probate. Informal probate is possible if a deceased's probate property is $200,000 or less. Property which is subject to probate is property owned in the deceased's name only; thus, the property owned jointly, property with beneficiary designations other than the estate of the deceased are not subject to probate. Both informal and formal probate are public proceedings requiring a lawyer. Formal probate is a complicated, time-consuming, and expensive process. Probate files are open to the public and public notice of the probate must be given in the local newspaper. This means that anyone can go to the court house and review the probate documents listing your assets, debts, and who will receive your property. Based on what they find, they may decide to assert a claim against your estate or contest the proposed distribution of your assets.

Death probate usually requires six months to a year to complete. It may take as long as two years. During probate, nothing can be distributed or sold without the court's approval. This means your survivors may be dependant upon the court for living expenses, sale of a residence, and the timing of distribution of their share of your property.

The expense of probate varies from state to state. If you own real property in more than one state, a probate process will be required in each state. In Wyoming, your administrator or personal representative is entitled to collect a statutory fees of approximately 2% of the total value of your probate estate for his or her services, and the lawyer handling the probate is entitled to another 2%. These fees are calculated on the gross value of your probate estate plus the earnings of the estate during probate without subtracting debts, mortgages, or other expenses. If your estate is contested, the court may approve legal and administration costs above the basic statutory fees.

Probate may be avoided by using a revocable or living trust, joint ownership, beneficiary designations, beneficiary deeds, pay-on-death accounts, and by gifts of property while you are still alive. However, you should not do you estate planning solely with the goal of avoiding probate. Joint ownership and beneficiary designations only postpone probate until the second death, create difficulties if you are ill or disabled, and may cause estate tax complications. A good estate plan should plan for incompetency to avoid living probate and consider the possibility of estate taxes and death probate on both the first and second death.