First Parish Milton
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TOPICS

- I. Estate Planning in General
- II. Charitable Giving During Life
- III. Charitable Giving Upon Death

I. ESTATE PLANNING IN GENERAL

Questions presented by estate planning:

- Who will make financial and medical decisions on my behalf should I be incapacitated?
- Who will take care of my children if I pass away?
- Who will receive my property upon my death?
- How will my property be handled after my death?
- How can I avoid probate and administrative costs?
- How can I make sure that I will have enough cash available to meet the needs of my estate?
- How can I help minimize my taxes?

Three basic levels of estate plans

- Level I Plan - Simple Estate Plan
- Level II Plan - Estate Plan with a single Revocable Trust
- Level III Plan - Estate Planning for a Taxable Estate
- Level IV Plan – When You Want to Save Even More Estate Taxes
- What level of estate plan is best for you will depend on your needs

LEVEL I PLAN

Simple Estate Plan

Level I Plan consists of:

- Durable Powers of Attorney
- Health Care Proxies
- HIPAA Information Release Authorization Forms
- Living Wills
- Wills

Durable Powers of Attorney

Power of Attorney

- A power of attorney is a document that appoints another person, called an attorney in fact, to act on your behalf.
- There are a wide variety of powers of attorney.
  - Powers of attorney can be general, meaning that the attorney in fact can do almost anything the original person could do.
  - Powers of attorney can be limited, meaning that the attorney in fact's powers may be limited to a specific purpose. (For example, I could appoint my accountant to act on my behalf solely for the purposes of helping prepare my income taxes.)
  - Powers of attorney can be durable, which means that their powers are unaffected by the incapacity of the person.
  - Durable powers of attorney can either be effective immediately, or can be springing, which means that they only become effective upon the person's incapacity.
- In this case, what we are proposing is a general durable power of attorney.

Powers one can grant to an attorney in fact:

- What are some of the powers that an attorney in fact might exercise on your behalf while you are incapacitated, under a general durable power of attorney?
  - buy or sell real property on your behalf;
  - buy or sell personal property for you;
  - trade in securities;
  - pay your bills and/or taxes;
  - operate your business;
  - have access to your safe deposit box;
  - purchase life insurance policies and name beneficiaries;
  - sue or defend a law suit on your behalf;
  - apply for governmental benefits on your behalf;
  - have access to your business and personal records;
  - etc., etc.

Fiduciary Duty

- With all this power, one may ask what is to prevent the attorney in fact of a General Durable Power of Attorney from emptying your bank accounts while you are incapacitated, and heading for Aruba?
- The attorney in fact is subject to a fiduciary duty, which means that the attorney in fact can only exercise his or her powers for your benefit.
- Any other use of the power is considered a breach of duty, and potentially a criminal act.

Health Care Proxies

Health Care Proxies

- Your Health Care Proxy (HCP) appoints a Health Care Agent to make any and all decisions relating to your health and medical care, should you be unable to make or communicate such decisions to other people.
- This includes the ability to select what type of medical treatment you will receive, and whether or not to withdraw life support in the event that you are dying with no reasonable hope of recovery.

Choice of health care agent

- Terri Schiavo case – it took 15 years for the Court to remove her feeding tube.
- As should be evident, one should give careful thought to your choice of health care agent. After all, you may end up trusting this person with your life.
- As should also be evident, you should also provide as much additional guidance to your health care agent as possible regarding what health care decisions you would want him or her to make on your behalf. Discuss with your health care agent various possible injury and illness scenarios, and what type of treatment you would or would not want those circumstances.

HIPAA Information Release Authorization Form

HIPAA Information Release Authorization Form

- The HIPAA Information Release Authorization Form specifically lists the individuals to whom you authorize the release of your protected medical information. HIPAA stands for Health Information Portability and Accountability Act.
- It is advisable to execute a HIPAA Information Release Authorization Form even if you only wish close family members to access your medical information, as some hospitals will even bar spouses and children from accessing such information without authorization.

Living Wills

Living Will

- A Living Will is a document that expresses your general intent that you desire that your life shall not be artificially prolonged should you have an incurable or irreversible condition, and that you be allowed to die a natural death with dignity.
- Living Wills are not binding legal documents in Massachusetts, but help provide your Health Care Agent with guidance regarding a very difficult decision.

Wills

Wills

- The purpose of your Will is to dispose of property held in your individual name upon your death. This property is also known as "probate property".
- Your Will also appoints a Personal Representative to help administer your estate, and a guardian and conservator to take care of any of your minor children. Children are considered minors until they attain age 18.

Probate Property

- Examples of Probate Property:
  - A bank account in your individual name would be probate property.
  - Jointly held property is not considered probate property
  - Property transferred by contract, e.g. a life insurance policy, is not considered probate property
  - Retirement accounts (such as your 401K or IRAs) are not considered probate property
  - Property held in a trust is not considered probate property
- The key inquiry is whether or not the court will have to take an active role upon your death to determine who should receive such property (based upon either your Will or the laws of intestacy).

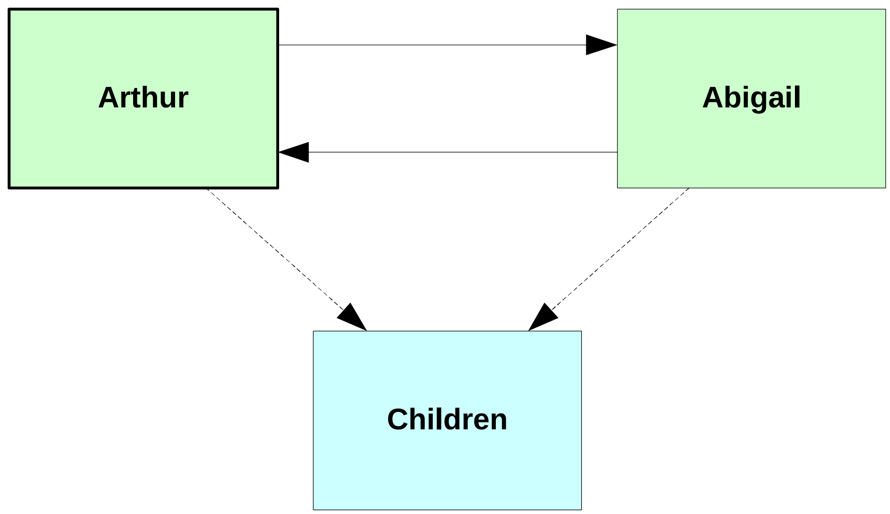
Intestacy

- If you die without a Will, your property will be distributed according to the laws of intestacy (MGL 190B:2-102). Surviving spouse will receive:
  - the entire intestate estate if:
    - **no descendant or parent** of the decedent survives the decedent; or
    - **all of the decedent's surviving descendants are also descendants of the surviving spouse** and there is no other descendant of the surviving spouse who survives the decedent;
  - the first $200,000, plus ¾ of any balance of the intestate estate, if no descendant of the decedent survives the decedent, but a **parent** of the decedent survives the decedent;
  - the first $100,000 plus ½ of any balance of the intestate estate, if there are any descendants of the decedent or the surviving spouse that are **not in common** with each other;
- This distribution may not properly reflect your wishes.
- Remainder to descendants per capita at each generation.

Disinheritance

- You can fully disinherit your children. Should you decide to do so, you may want to consider an anticontest clause
- Elective Share: You cannot fully disinherit your spouse. Your spouse is entitled to a portion of your property, even if you do not want to give him or her anything upon your death (MGL 191:15)
  - If you have living descendants, your spouse will be entitled to 1/3 of your personal property and 1/3 of your real estate (First $25,000 outright, the rest in a life estate)
  - If you do not have living descendants, he or she will be entitled to $25,000, plus ½ of your remaining personal property and ½ of your remaining real estate in a life estate.
  - In addition, special rules may apply to your retirement assets.

How do people generally dispose of their property in their Wills?



- Most people have their Wills give all their property to their spouse, if he or she survives them.
- If their spouse does not survive them, all of their property is transferred to their children and more remote descendants, by right of representation
- "By right of representation" means that in the event that any of your children are then deceased, his or her descendants will take in his or her place.

LEVEL II PLAN

Estate Plan with a single Revocable Trust

Level II Plan consists of:

- All the same documents as a Level I Plan:
  - Durable Powers of Attorney
  - Health Care Proxies
  - HIPAA Information Release Authorization Forms
  - Living Wills
  - Wills
- But, in addition, a single Revocable Trust

Revocable Trust

What is a Trust?

- A Trust is a fiduciary relationship in which a Settlor, the person who sets up the Trust, gives property to Trustees to hold for the beneficiaries of the Trust, in accordance with the trust terms.
- Let me give an example. If I (the Settlor) give $100 (the property) to you (the Trustee) to hold for my son (the beneficiary) for the next week (the trust terms), that is an example of a trust. I’m giving something to someone to hold for the benefit of someone else in accordance with my instructions.

Revocable Trust vs. Irrevocable Trust

- In this case, we are talking about a Revocable Trust, which means that you as the Settlor can revoke or amend the Trust at any time.
- You may also withdraw any part or all of the property of your Revocable Trust at any time during your life.
- A Trust may also be Irrevocable, which means that it cannot be changed once created.

Why include a Revocable Trust in your estate plan?

- One reason is that a Trust allows you to continue to continue to control your property after you die
- If your Will gives your property to your children after your death, they will receive full access to such property upon attaining age 18 (the age they are no longer considered minors).
- At this time, they will be free to spend this money on anything they like (for example, Porsches, boats and expensive parties).
- Property could be held in an UTMA or UGMA account until age 21, but no later without a trust.

A Trust can hold property for your children until they are mature enough to handle such property

- Many parents do not feel comfortable with giving their children full access to the property so soon.
- Oftentimes, they want a Trust to hold such property for the benefit of their children, until they reach an age which the parent deems appropriate.
- Example:
  - Akbar has an only child, named Abraham. Akbar and his wife set up a Level II Plan.
  - Upon the death of the survivor of Akbar and his wife, the property of the Trust will be held for the benefit of Abraham, with discretionary distributions available for his health, education, support in reasonable comfort, and maintenance.
  - Upon attaining age 30, such child may withdraw ½ of the remaining trust property.
  - Upon attaining age 35, he may withdraw the remainder.

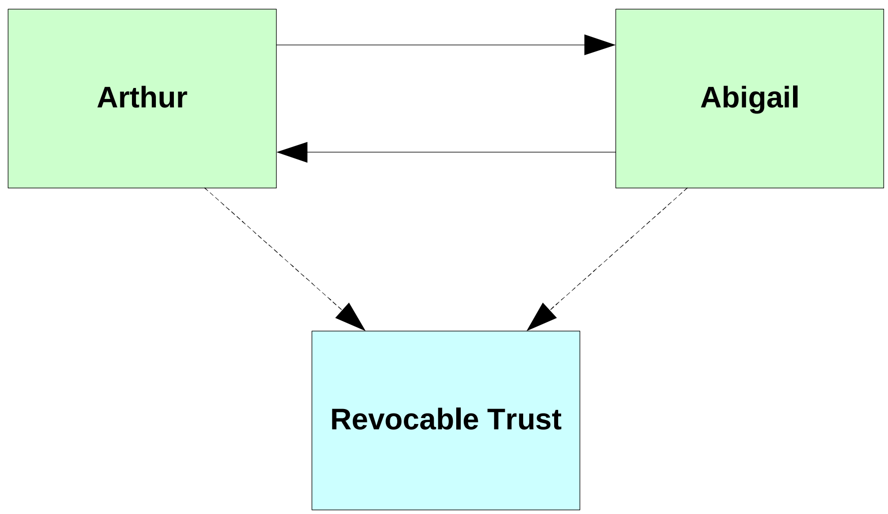
A Trust can help provide asset protection

- In addition, a Trust created by you will help shield any property it holds from any potential creditors of your children while it holds such property. This includes to a certain degree divorcing spouses of your children.
- For this reason, some people like to hold property in trust for their children's entire lifetimes, to make sure that a nest egg will always be available for them, regardless of what happens during their lives.

Any property held in your Trust upon your death will avoid probate

- Any property transferred to a Trust prior to your death will avoid probate.
- Probate is the often lengthy and cumbersome process by which the court system determines who should receive your probate property (property in your individual name) upon your death.
- The probate process generally takes at least a year, during which time your beneficiaries will generally not be able to receive your property.
- The probate process can also be costly in terms of attorney's fees.

How do people generally dispose of their property in a Level II Plan?



- Most people have their Wills give all their property to their spouse, if he or she survives them.
- If their spouse does not survive them, all of their property is transferred to their joint revocable trust, to be held for the benefit of their children.

LEVEL III PLAN

Estate Planning for a Taxable Estate

Level III Plan consists of:

- All the same documents as a Level I Plan:
  - Durable Powers of Attorney
  - Health Care Proxies
  - HIPAA Information Release Authorization Forms
  - Living Wills
  - Wills
- In addition, Credit Shelter Trusts for both husband and wife

Federal Estate Tax

- If you die with more than $12,920,000 in your taxable estate in 2023, the federal government will impose a federal estate tax upon your estate at a 40% rate.
- Your taxable estate is different than your probate estate. Your taxable estate includes all of your property
  - Property held in your revocable trust will be included in your taxable estate
  - The death benefits for life insurance on your life owned by you will be included in your taxable estate
- The $12,920,000 federal exemption is indexed for inflation.
- Sunset to $6,460,000 in 2026.

Massachusetts Estate Tax

- If you die with more than $1,000,000 in your taxable estate in 2023, the Commonwealth of Massachusetts will also impose a Massachusetts estate tax upon your estate.
- The $1,000,000 Massachusetts exemption is not currently scheduled to increase over time.

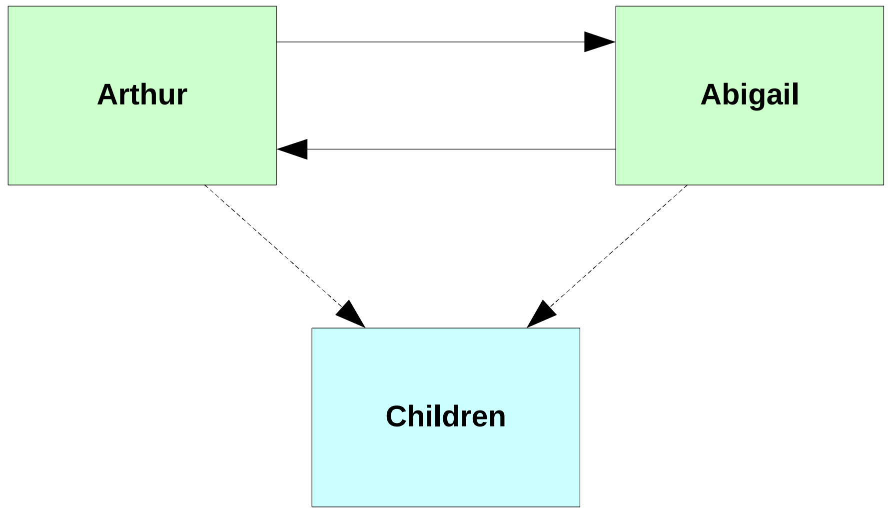
How much Massachusetts estate tax will be due?

Taxable Estate	MA estate tax
1 M	$ -
1.5 M	$ 64,400
2 M	$ 99,600
2.5 M	$ 138,800
3 M	$ 182,000
3.5 M	$ 229,200
4 M	$ 280,400
4.5M	$ 335,600
5 M	$ 391,600
5.5 M	$ 450,800
6 M	$ 510,000
7 M	$ 638,000
8 M	$ 773,200
9 M	$ 916,400
10 M	$ 1,067,600
11 M	$ 1,226,800
12 M	$ 1,386,800
13 M	$ 1,546,800
14M	$ 1,706,800
15 M	$ 1,866,800
20 M	$ 2,666,800

Marital Deduction

- In addition to federal and Massachusetts exemptions, one also receives an unlimited marital deduction for any property transferred to your U.S. citizen spouse
  - QDOT required for non-citizen spouses.
- This means that you can give all your property to your spouse upon your death, without having to pay any estate taxes.
- If one did this, however, one would miss out on the opportunity to take advantage of your federal and Massachusetts exemptions, and additional taxes would be due upon the death of the survivor among you.

Level I Plan may result in greater taxes



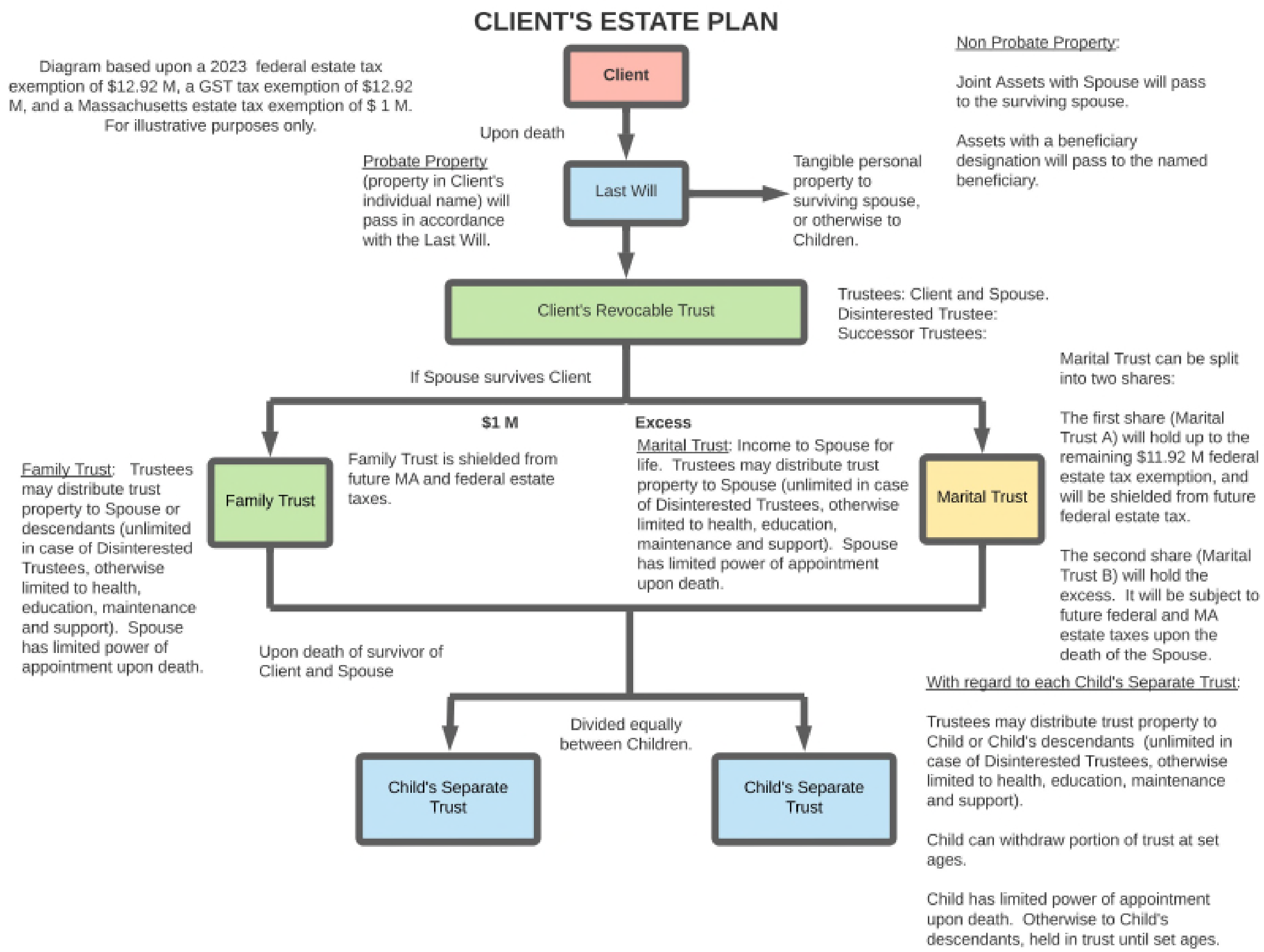
- Assume combined property of $2 Million
- Each spouse gives all of his or her property to his or her spouse if he or she survives him
- If both Arthur and Abigail die in 2023, **no federal estate taxes will be due**, and Massachusetts Estate Taxes will be **approximately $100,000**.
- Same result with Level II Plan.
- With Level III Plan, upon second death, **no federal estate taxes will be due**, and no Massachusetts estate taxes will be due.

Credit Shelter Trusts

How do Credit Shelter Trusts save you taxes?

- Credit Shelter Trusts are individual revocable trusts for both yourself and your spouse, with special provisions dividing themselves into separate shares in the event you predeceases your spouse:
  - The amount of the Massachusetts exemption ($1,000,000 in 2023) is set aside as the “Family Trust”, to be held for the benefit of your spouse and children.
  - The difference between the federal exemption and the Massachusetts exemption ($11,920,000 in 2023) is set aside as “Marital Trust A”, to be held for the benefit of your spouse.
  - Any additional property held by the Trust will be set aside as “Marital Trust B”, to be held for the benefit of your spouse.
- By setting aside the amount of the federal and Massachusetts exemptions upon your death, you and your spouse can fully utilize your exemptions

Standard Credit Shelter Trust



Upon death if your spouse survives you

- Family Trust: Trustees may distribute trust property to Spouse or descendants Spouse has limited power of appointment upon death.
- Marital Trust: Income to Spouse for life. Trustees may distribute trust property to Spouse. Spouse has limited power of appointment upon death.

Upon death of survivor of Client and Spouse

- Trust can either be held in a single POT trust for the benefit of all the children or can split into separate trust for each of the children.
- POT Trust: Held as a single trust for the benefit of the children until the youngest one turns age 23. This way one can be assured that all of the children have had their college taken care of. Thereafter, POT Trust splits into shares for children as well.
- With regard to each Child's Separate Trust: Trustees may distribute trust property to Child or Child's descendants. Child can withdraw portion of trust at set ages. Child has limited power of appointment upon death. Otherwise to Child's descendants, held in trust until set ages.

Generation Skipping Provisions

- Example: Arthur had a son named Akbar, who had a son named Abraham.
- As we know, if Arthur dies with a taxable estate, estate taxes will be due on his estate. Under the above estate plan, ½ of the remaining property of Arthur's Family Trust will be distributed to Akbar. If Akbar then dies with a taxable estate, his estate will also have to pay estate taxes.

Generation Skipping Provisions

- So, Arthur has an idea: Why not simply set aside ½ of the property of his Trust after his and Abigail's deaths for the benefit of his grandson, Abraham, instead of Akbar? This way, he could skip the need for Akbar to have to pay estate taxes on the property. Akbar could still receive discretionary distributions from Abraham's trust.
- The reason this will not work is because the federal government imposes a generation skipping transfer tax on transfers to your grandchildren or more remote descendants for transfers of more than the generation skipping transfer tax exemption ($11,920,000 in 2023).
- Arthur still has a good idea. One just has to limit the amount set aside for his grandchildren to the amount of the generation skipping transfer tax exemption.

Generation Skipping Provisions

- A generation skipping transfer trust seeks to shield up to the amount of the generation-skipping transfer tax exemption from estate tax, so that it is not counted when your children pass away.
- So in our example, Arthur could set aside up to $11.92 M in trust for his descendants, and if his children did not have the ability to demand the trust assets the trust would not be subject to estate tax when his children die.
- The amount in a generation skipping transfer trust will only be subject to estate tax once it is distributed out of the trust to a beneficiary that passes away.
- However the trust cannot last forever. There is a rule against perpetuities that indicates when the trust will have to terminate.

Gifting and Irrevocable Trusts

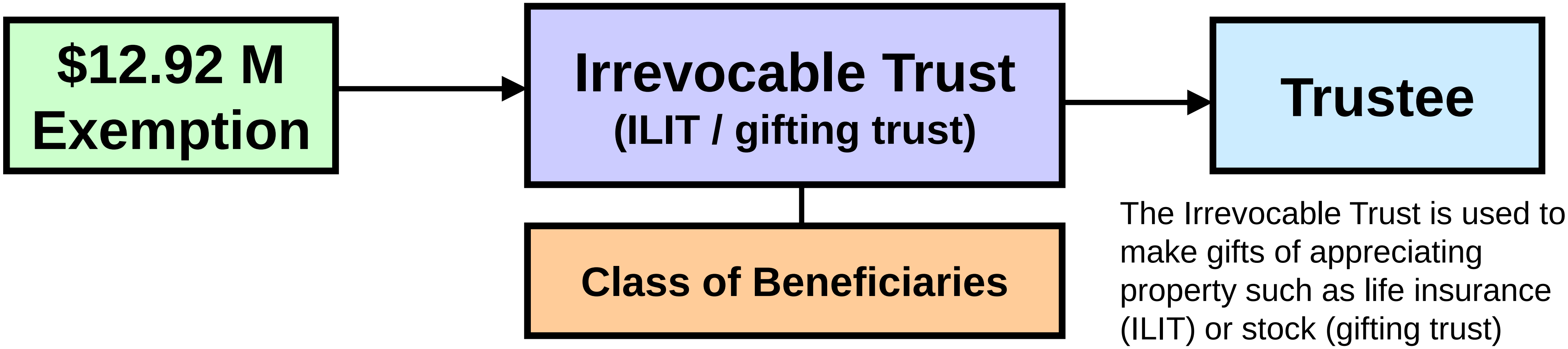
Federal Gift Tax Exemption

- $12,920,000 exemption for Lifetime Gifts
- Counts Against Estate Tax Exemption at Death
- Note: $17,000 Annual Exclusion for Gifts in Addition to $12,920,000 Million Lifetime Gift Tax Exemption.

Gifting Strategies

- $17,000 Annual Gift Tax Exclusion/$34,000 for "Gift-Splitting" with Spouse
- $12,920,000 per Donor Lifetime Exemption from Gifts
- "Qualified Transfers" for Tuition Expenses or Medical Expenses are not Taxable
- Gifting Vehicles
  - Outright Gifts
  - FLPs and LLCs
  - UTMA Gifts (Age 21)
  - Section 529 Plans
  - Trusts
- There is however no step up in basis upon death.

Irrevocable Trust



<u>Advantages:</u>

- Use of exemption now
- Tax-free shift of future appreciation
- Trust gives protection for beneficiaries
- Customized provisions
- “Defective” for income tax purposes?
- Discount may be possible for lack of marketability and control for a gift of minority interest in business

<u>Disadvantages:</u>

- Irrevocable
- Need for present interests (Crummey notices)
- Bad deal if gifted asset depreciates
- Possible estate/gift tax repeal

Additional Strategies

Additional Strategies

- Declarations of Homestead
- Nominee (Realty) Trusts
- FLPs (family limited partnerships) and LLCs (limited liability companies)
- Buy Sell Agreements
- GRATs (Grantor Retained Annuity Trusts)
- QPRTs (Qualified Personal Residence Trusts)
- IDGTs (Intentionally Defective Grantor Trusts)
- CRTs (Charitable Remainder Trusts), etc.

II. Charitable Giving During Life

General Charitable Giving

- Donations to qualified charities are tax deductible for both income and estate tax purposes.
  - IRC 170(c) Donor can deduct up to 60% of AGI to qualified charity on Donor's income tax returns.
  - IRC 2055 Donor can deduct assets contributed upon death to qualified charity on Donor's estate tax returns.
  - IRC 2522 Donor can deduct assets contributed during life to qualified charity on gift tax return.
  - IRC 501(c)(3) A qualified charity does not have to pay income taxes.
- Estate and gift taxes are both "transfer" taxes
- Churches are considered qualified tax exempt organizations without the need to seek formal IRS recognition of their tax exempt status.
- Can bunch up donations in order to maximize tax impact in certain years.

Qualified Charitable Donations (QCD)

- At age 70 ½ one can start donating up to $100K from your IRA per year to charities instead of taking them as required minimum distributions.
- Ordinarily at the appropriate age, IRA owners are required to start taking required minimum distributions from their IRAs and recognizing such distributions as taxable income.
  - The age one can start donating is still 70 ½ even though the RMD start age is rising to 72 and eventually 73.
- Because a qualified charitable donation goes directly to the charity without passing through your hands, the charity will receive the entire amount of the gift and not an after tax amount.
- Currently cannot make QCDs to private foundations, donor advised funds, or supporting organizations.

Gifts to Charitably Minded Children

- If you are in a low tax bracket and have adult children in a high tax bracket one might consider gifting assets to your children so they can make gifts to charity and save taxes for themselves.

III. Gifts upon Death

Including a charity in your estate plan

- Can devise assets to charity
- Can name charity as a beneficiary of retirement assets (saves income and transfer taxes)
- Can name charity as end limitation beneficiary.

CRTs

- CRTs provide regular payments to individual beneficiaries for a period of time and at the end of the trust distribute the remainder of the trust to a charity.
- CLTs provide regular payments to a charity for a period of time and at the end of the trust distribute the remainder of the trust to an individual.
- Can provide an upfront tax deduction.
- May be useful to provide benefits to both an individual during their lifetime and also a charity.
- Can be a unitrust or annuity trust.
- Reverse of a CLT.

501(c)(3) organizations

- A 501(c)(3) organization is an organization that is exempt from paying income taxes.
- To be a 501(c)(3) organization the organization must:
  - Be organized and operated exclusively for religious, charitable, scientific, public safety, literary, education, etc. purposes.
  - Must be for public not private purposes.
  - Cannot be a political organization.
  - Cannot engage in activities not in furtherance of its exempt purposes.
- The 501(c)(3) must file a Form 1023 application. Exception: churches automatically qualify as a 501(c)(3).
- The 501(c)(3) can be an unincorporated association, trust, LLC or corporation.
- All 501(c)(3)s are private foundations unless they qualify as a public charity. Public charities are subject to less strict rules.
- Requirements to qualify as a public charity provided in IRC 509:
  - Church, School, Hospital,
  - A publicly supported organization
  - A Gross Receipts organization,
  - A Supporting Organization, or
  - A Public Safety Organization.

Private Foundations

- Private foundations are a type of 501(c)(3) organization.
- Gifts to a private foundation should qualify for income / gift / estate tax charitable deductions.
- Limitations on private foundations:
  - Excise tax on investment income
  - Taxes on self dealing
  - Tax on failure to distribute income
  - Limitation on excess business holdings
  - Limitation on investments that jeopardize charitable purposes
  - Tax on certain expenditures
  - Income tax deductibility more limited
- In essence a private foundation must distribute not less than 5% of the FMV of its non charitable assets each year.
- The foundation determines which charities to distribute assets to.
- Private foundations have high administrative expenses to maintain.
- Generally it is not worth creating a private foundation worth less than $3M.

Donor Advised Funds

- A donor advised fund is essentially an account maintained and operated under an already existing sponsoring public charity. The public charity will be a 501(c)(3) organization.
- Gifts to a Donor Advised Fund should qualify for income / gift / estate tax charitable deductions.
- Once the donor makes the contribution, the sponsoring public charity has legal control over it.
- However the donor or the donor's representative retains advisory privileges with respect to the distribution of funds and the investment of assets in the account. Although the sponsor does not have to absolutely follow the donor's wishes it generally will.
- The benefit is that the donor does not have to take care of the paperwork to maintain the fund.
  - Because the sponsoring organization is a public charity, they are not subject to the same rules and limitations of private foundations.
  - They also have lower administrative costs and do not have to file separate tax returns or reports.
- Many donor advised funds will let the donor name at least one more generation of advisors, although this is not indefinite.

Further Questions?

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