FERRIS FINANCIAL, LLC

HELPING YOU PLAN, PROTECT & PROSPER

Overview

Regardless of your level of wealth, the failure to establish an estate plan can be detrimental to your family. A properly structured estate plan helps ensure that your family and financial goals are addressed during your life, if incapacitated, and after your death. The following provides an introductory discussion regarding essential planning individuals should consider, as well as an overview of lifetime gifting strategies and long-term trust planning.

Essential Documents

The following planning documents should be considered regardless of whether an individual is married or single.

Last Will and Testament

A will directs how you want your assets distributed upon your death. Without a will, your property would pass as required under your state's intestacy statutes. State law may not provide the inheritance scheme you would choose for your family, and could also increase your exposure to federal estate taxes.

In addition to directing the disposition of your property, a will can enable you to:

- Name an executor, avoiding the trouble and cost of a court-appointed administrator.
- Avoid bonding costs.
- Avoid annual reporting/accounting to the probate court.
- Name a guardian for minor children, substantially eliminating the likelihood of a court-appointed guardianship.
- Protect the children's inheritances in the event your surviving spouse should remarry.
- Retain assets in trust if distributions to your heirs at your death would be inadvisable.

For high net worth married couples, a will, if structured properly, also can help assure federal estate tax benefits are preserved for the couple's estates. Estate tax-efficient wills allow a married couple to take full advantage of the unlimited marital deduction and the federal estate tax exemption ($11.18 million per individual in 2018, as indexed for inflation) of both spouses. Allocation of the first-to-die spouse's exemption amount to a trust may reduce estate tax for the couple's combined estate, provide asset protection and allow control and management by a trustee, while still benefitting the surviving spouse and children.

For couples with more modest estates, estate tax-efficient wills may not be as advantageous from a total federal tax perspective as an "all-to-spouse" will, taking into consideration the unlimited marital deduction, the potential portability of a deceased spouse's unused "applicable exclusion amount" (as discussed below), and the opportunity to have appreciated assets receive a step-up in tax basis at both spouses' deaths (which could help reduce the heirs' capital gains tax exposure).

Revocable Living Trust

A revocable living trust (RLT) is an arrangement by which a person (the grantor) transfers ownership of property into a trust during one's lifetime. An RLT can be used as a substitute for a will in many respects by providing for the distribution of assets upon the grantor's death. Unlike a will, a revocable living trust can be established to govern the distribution and use of the trust assets during the grantor's lifetime, which can make it a useful planning tool in the event the grantor becomes incapacitated. In essence, the trust is like a rulebook (which can be modified or revoked by the grantor during lifetime) for how the grantor's assets are to be handled while alive and after death.

Establishing an RLT may provide the following benefits:

- **Avoidance of Probate.** Probate is the legal process for transferring property upon death. Assets owned in an RLT do not pass through the probate process, potentially enabling a faster and less costly method for transferring assets upon death than by a will, which would require probate and sometimes court supervision. An RLT also can be especially useful in avoiding multiple probate proceedings when an individual owns real estate or other property in multiple states.
- **Privacy Preservation.** At an individual's death, when assets are passed to the heirs through probate under a will, probate may expose details of an estate to the public through public probate court filings. In contrast, trusts allow the transfer of assets to remain private within the constraints of the trust document.
- **Segregation of Assets.** An RLT may be useful for married couples with substantial separate property acquired prior to the marriage. In community property states, the trust can help segregate those assets from their community property assets.
- **Estate Tax Minimization.** An RLT does nothing to save estate or income taxes during life, but provisions can be included in the trust, as with estate tax-efficient wills, to take advantage of estate tax exemption amounts at death.

Durable General Power of Attorney

A power of attorney is a document that allows a person (known as the "Principal") to appoint another person or organization to handle affairs while the Principal is unavailable or unable to do so. The person or organization the Principal appoints is referred to as an "Attorney-in-Fact" or "Agent."

A general power of attorney can grant the agent limited or broad powers as specified in the document to manage the principal's financial affairs and property. Some of the powers that may be granted include:

- Handling banking transactions and transactions involving U.S. securities.
- Entering safety deposit boxes.
- Buying and selling property.
- Purchasing life insurance.
- Settling claims.
- Entering into contracts.
- Buying, managing or selling real estate.
- Filing tax returns.
- Handling matters related to government benefits.
- Maintaining and operating business interests.
- Making gifts and consenting to splitting gifts made by the principal's spouse.
- Making transfers to RLTs.

Health Care Power of Attorney

A Health Care Power of Attorney allows the principal to designate an agent who will have the authority to make health care decisions on the principal's behalf in the event the principal is rendered unconscious, mentally incompetent or is otherwise unable to make such decisions.

A HIPAA (Health Insurance Portability and Accountability Act) Authorization also is advisable. It allows medical providers to release a person's protected medical information to another person. Individuals may include the HIPAA language in the Health Care Power of Attorney, or may use a freestanding document. If your state has a HIPAA Authorization form that has been published or approved by a state regulatory agency, consider using the approved form because medical professionals in your state will be more likely to recognize the form and release the information when requested.

Living Will / Advance Directive

A living will, also known as an advance directive, is a legal document that a person uses to make known one's wishes regarding life prolonging medical treatments. The person creating the living will (the declarant) indicates which treatments the declarant does or does not want applied in the event the declarant suffers from a terminal illness or is in a permanent vegetative state. A living will does not become effective unless the declarant is incapacitated. Until then the declarant will be able to direct one's own treatments.

Estate Planning Strategies and Considerations

Making Lifetime Gifts

Many individuals and married couples make gifts to their children and other family members. Lifetime gifts may allow the person making the gift (the donor) to observe how the recipients (the donees) will handle the money. Accordingly, by making lifetime gifts the donor can help guide the donee on sound money and business management skills. Gifts also can help reduce a donor's taxable estate if desirable. However, making gifts in excess of the donor's lifetime gift tax exemption amount ($11.18 million in 2018) may result in the imposition

of gift taxes. A gift tax is a federal tax on the transfer of property by one individual to another where the person making the gift receives nothing in return.1

Annual gifts. Each year, a donor can gift up to a specified amount ($15,000 in 2018) to each of an unlimited number of donees without triggering federal gift taxes by using what is commonly referred to as the "gift tax annual exclusion." The annual exclusion amount is indexed for inflation, but only adjusted in $1,000 increments. Through "gift splitting," married couples can use their combined annual exclusions for a given donee even if only one spouse actually transfers property to that donee.

Only gifts of a "present interest" are eligible for the annual exclusion. Gifts of a "future interest" are ineligible. If a recipient receives a gift with no strings attached, the gift is of a present interest. If there are conditions on the gift or if there is a delay in the enjoyment of the gift, the gift is a future interest gift. A gift to a trust is a gift of a present interest only if:

(1) the beneficiary has the present right to trust income,

(2) the beneficiary has a right to withdraw the amount of the gift from the trust and is given timely written notice of such right; or

(3) the trust is for the exclusive benefit of a minor and meets certain requirements.

Applicable Exclusion Amount. Every U.S. citizen is permitted a "unified credit" that allows the individual to transfer a certain amount of assets free of federal transfer taxes during life or at death. If a donor makes gifts to a donee during any given taxable year that exceed the annual exclusion amount, the donor can reduce any potential gift tax by applying all or a portion of his or her unified credit. At death, the executor of the decedent's estate will reduce the amount of estate tax due by any unified credit not used during the decedent's life. The amount of assets the credit effectively exempts is referred to as the "applicable exclusion amount." The applicable exclusion amount for gift and estate tax purposes is $11.18 million in 2018. The entire amount can be gifted during life, if desired.

Medical and Educational Gifts. Direct payment by an individual to a provider of qualified educational or medical expenses for the benefit of another individual does not constitute a taxable gift. The definition of educational expenses only includes tuition paid directly to the educational institution, not room and board, books, etc. As for medical expenses, IRS regulations describe exactly what types of expenses will be treated as qualified medical expenses.

Outright Gifts and Bequests vs. Long-Term Trusts

Rather than making an outright gift (during life) or bequest (upon death), many individuals choose to place assets in long term trusts for the donee's benefit. Assets held in trust are distributed according to the trust terms. As long as the trust remains in effect, assets can generally be protected from creditors, litigation and divorce, as well as from mismanagement by the recipient. If incorporated into the terms of the trust, distributions can be structured to either encourage or discourage certain behavior. For example, the grantor of a trust could provide that distributions be made upon a beneficiary graduating from college or after holding a job for a certain number of years. A grantor also could require distributions be withheld in the event of a beneficiary's impending bankruptcy or for proven or suspected use of an abusive substance.

[1] Connecticut and Minnesota also impose a state-level gift tax in addition to the federal gift tax, with exemption amounts substantially less than the federal exemption amount.

- If desired, a beneficiary of a trust can serve as a trustee (or co-trustee) of that trust; however, if a beneficiary/trustee will be granted powers to make discretionary distributions of trust assets to oneself, such powers should be limited to an ascertainable standard, more specifically for their health, education, maintenance and support, to keep the trust's assets out of the beneficiary's taxable estate. From an asset protection standpoint, a trustee/beneficiary with rights to make discretionary distributions to one's self may expose the beneficiary's rights to claims of creditors. In contrast, if rights are granted to an independent third party trustee to make discretionary distributions to the trust beneficiaries, trust assets may be more effectively protected from the claims of the beneficiaries' creditors. Moreover, unlike a trustee/beneficiary, an independent trustee can be granted unlimited discretion to distribute assets to a beneficiary without causing the trust's assets to be includible in the beneficiary's taxable estate.

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