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Consider This!

Timely News and Information About Estate Planning and Family Wealth Counseling Strategies

The Big Shift; Get In Gear

The greatest intergenerational transfer of wealth has begun to occur. And many people aren't ready.

Getting your finances in order and creating a solid estate plan can be about as much fun as dental surgery. But ignoring the subject, as many Americans do, can lead to even greater pain.

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What you are about to read illustrates how our law firm explains—in lay person's language—the secrets of how to keep wealth in the family and leave a legacy for loved ones through effective estate planning.

At Price & Farrington, PLLC, we provide you with the information you need to make well-informed decisions about your personal planning and how that planning can most effectively be implemented to accomplish your goals.

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is presented by

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The Big Shift; Get In Gear

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To occur. And many people aren't ready.**

THE LAY OF THE LAND

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Each year, many Americans die without having drawn up a will or trust, documents specifying how they want their property to be divided among their heirs. Dying intestate, as it's called, can lead to unexpected consequences, with judges and local laws dictating the distribution of your assets in ways that you would not have chosen. Doing nothing also can trigger epic family battles that could easily have been avoided.

"You can save a lot of money and prevent all kinds of disasters from occurring" merely by taking some of the most basic and simplest steps, says Sidney Kess, a New York lawyer and certified public accountant.

But even people who should know better often fail to get their own house in order. For example, Mr. Kess recalls a certified public accountant who died at age 52 without having done any estate planning--and without having told his sister, who was his primary heir, where any important papers or financial documents were located. "It cost thousands of dollars" to undo the damage, Mr. Kess says.

The stakes have never been higher. Over the next couple of decades, the biggest intergenerational transfer of wealth in U.S. history is expected to occur, with baby boomers inheriting trillions of dollars amassed by their parents during the long running bull markets in stocks and housing. But getting children or their parents to sit down to discuss the subject can be exceeding difficult. Even bringing up the issue is considered taboo in many households.

"When people are young, they feel immortal--and when they get older, they just don't want to talk about it," says Martin Nissenbaum, national director of personal income-tax planning at Ernst & Young in New York. "So starting the process early makes it easier psychologically." Moreover, he says, "there are always cases where people die sooner than they anticipated, and having an estate plan in place will be a great comfort to their survivors."

Estate planning definitely is not a field for amateurs. The rules can be so mindnumbingly complex, especially for medium-size and large estates, that you really need to look for qualified legal and accounting expertise.

Early in 1999, it looked like a few tax-saving techniques might disappear. The Clinton administration's proposed budget recommended killing or at least limiting a few highly popular estate-

planning techniques, such as family limited partnerships, that can help cut a tax bill. But those efforts appear to have fizzled, leaving Americans with a wide range of antitax weapons.

For people who want to get started, or for those wondering whether what they've already done is sufficient, here's a rundown on some of the essentials of estate planning.

WHO IS AFFECTED?

Everyone. Because everyone needs to plan. But Treasury Department officials say only about 2% of the people who die each year in the U.S. leave estates large enough to worry about being subject to the estate tax. For example, in a recent year there were only about 42,500 taxable estate-tax returns filed last year out of a total of nearly 2.4 million deaths, a Treasury official says.

The 2001 tax law excludes $1,000,000 per person in 2002 and 2003, 1,500,000 in 2004 and 2005, $2,000,000 in 2006-2008 and $3,500,000 in 2009. The law repeals estate taxes in 2010 and reinstates them in 2011. It is unlikely that estate taxes will ever be repealed. Changes in the 2001 tax law are anticipated in the coming years. In the meantime, if one spouse dies, the other spouse typically can keep the entire estate, tax-free, at least on the first spouse's death..

But for those who are affected, the tax bite is large, which explains why top estate-tax consultants are in great demand. The Treasury expects to continue to collect many billions in estate-tax revenue in the coming years. The top federal marginal rate can be as high as 50%. Depending on where you live, (Washington state, for example) there are also state estate taxes.

STEP ONE: WRITE A WILL OR TRUST

This seemingly obvious advice is ignored by many people partly because it requires making what may be difficult and delicate choices, such as sorting out who will inherit what share of the family fortune, or who will get certain valuable property and family heirlooms. Whatever the explanation, failing to have an attorney draw a will or trust is usually a cruel thing to do to your family and friends.

In most cases, paying an expert to prepare your will should be fairly inexpensive. Some lawyers are eager to write wills at relatively low cost because they hope they will eventually be named to handle the probate estate.

When putting together your will or trust, watch out for some classic mistakes. For example, some people assume it's enough to name their child as their heir--without bothering to consider what would happen if they and their children all die at the same time, such as in a plane or car crash. Always be sure to name alternatives--both as heirs and guardians for children.

UPDATE YOUR PLAN

If you already have estate planning documents in place, take a fresh look at them, particularly in

light of the changes introduced in recent tax laws. The plan you carefully drew up 5 or 10 or 15 years ago may now be meaningless because of family deaths, divorces, births, adoptions or changes in your own financial condition. In some cases, failure to update a plan can create just as much mischief as not having drawn one up at all.

BE GENEROUS

The law allows you to give away as much as $11,000 a year, tax-free, to anyone you choose. It can be a child or a friend or even a perfect stranger. There are no limits: You are allowed to give that amount to as many people as you want each year. If you're married, you and your spouse can each give away $11,000, or a total of $22,000 per couple, to anyone.

You don't have to worry about paying gift taxes, and the lucky recipients don't have to worry about paying income taxes. It's one of the few truly simple breaks in the tax code--and a great way for wealthy people to transfer large amounts of money out of their taxable estates each year.

While this provision is well known, there are other, lesser-known ways to give away even more than that, tax-free. The law allows you to pay someone else's qualified tuition or medical expenses. Those payments don't count toward the $11,000 a year limit; there is no ceiling to how much you may pay. Just be sure to pay those expenses directly to the school or health-care provider, rather than handing over a check to the recipient to pay the bills. With some private schools now costing more than $25,000 a year, this is a provision well worth considering.

To help pay for college expenses, you might also want to consider using a qualified state tuition program. Such programs provide both an estate tax and an income tax benefit because in a typical program anything you contribute is not included in your estate, the income is tax-deferred and the distributions come out tax-free.

CONSIDER A POWER OF ATTORNEY

This is an extremely valuable tool, but one that requires great care because it can be so powerful. A power of attorney authorizes someone else (your "agent") to act on your behalf, including writing checks against your bank account. You don't have to give a lawyer your power of attorney; you can give it to anyone. But be careful to choose someone you trust completely. In the wrong hands, it can be your undoing.
Watch your language. Lawyers often recommend inserting wording that makes it a "durable" power of attorney, which means its power will remain valid even if the person who wrote it becomes incapacitated. In some states, a power of attorney is automatically considered durable unless stated otherwise.

And if you want to allow gift giving by the person you're empowering, be sure to say so in writing. Otherwise, you may face unpleasant challenges from family members and, even more ominously, the Internal Revenue Service. Also, spell out if you want to impose limits on the size of

gifts to be made, or to whom they may be made. Finally, remember that even the most carefully drawn power of attorney is not a substitute for a will or trust.

MAKE LISTS

Make sure you have a comprehensive list of where all of your important documents are located. It doesn't do any good to prepare or update your plan regularly if you forget to tell anyone where you keep it. If you store the only copy in your safe-deposit box, or in another secure location, make sure another person has access to it upon your incapacity or death.

Your inventory should also list where your safe-deposit box is located and where you keep the keys. With the proper documentation, the bank can always drill open a locked box if the keys are missing, but that can be costly to your agent or your heirs.

Other items to include on your list:

- The banks and other financial institutions where you have accounts, with all of your account numbers.
- Insurance policies and account numbers.
- Credit cards.
- Names and phone numbers of your lawyer, accountants, investment managers and any other key advisers you rely on to manage your finances.
- Important identification numbers, such as your Social Security number.
- Details of any tax-deferred accounts, such as individual retirement accounts, as well as the names and addresses of your beneficiaries.
- Location of your income-tax returns for each of the past three years, as well as any gift-tax returns you may have filed.

TRUST TRUSTS

Some people assume trusts make sense only when you don't really trust your heirs. That certainly can be an important reason. But there are many other reasons to consider trusts, such as to cut taxes. While some of these techniques are used primarily by the very wealthy, you don't have to be Bill or Melinda Gates to profit from these tools.
Some basic types of trusts are "revocable," which means they may be amended or terminated anytime you want. Others are "irrevocable," which means they are set in stone and can't be altered after being created.

Many people, both wealthy and not-so-wealthy, set up a "living trust" to hold their assets. A revocable living trust is popular as a way to help your heirs assist you in managing your assets while you're alive, if necessary, and avoid the complexities and expenses of probate after you die. Another idea is a life-insurance trust, where a life-insurance policy is put into an irrevocable trust to benefit your children or spouse, or both.

Another type of trust, known as a qualified personal residence trust, enables you to remove the value of your home from your estate.

There also are ways to transfer expected future gains on your securities or other assets, such as your stake in a closely held business. Consider a grantor retained annuity trust, or GRAT, where you typically place property into the trust and retain the right to receive an annuity during the trust's term.

One of the most common types of trusts is a bypass trust, also called a credit-shelter trust. It enables each spouse to take full advantage of the basic estate tax exclusion ($1,000,000 per person in 2002 and 2003; $1,500,000 in 2004 and 2005).

Another popular technique is the qualified terminable interest property trust, or Q-TIP, which essentially gives a surviving spouse the right to all trust income and, in some cases, access to principal, too. But when that spouse dies, the assets go to beneficiaries named by the person who set up the trust; yet those assets are included in the estate of the surviving spouse, thus deferring payment of the estate tax.

For people interested in charitable giving, there are many types of trusts to consider. Among these is a charitable remainder trust, which enables you to leave assets to your favorite college, church or some other charity while getting a steady stream of income as long as you live. That contrasts with a charitable lead trust, which pays a charity a certain amount of income from the donated property for a certain time period. After that, the principal passes to your beneficiaries.

There are trusts for minors (I.R.C. §2503(c) and 2503(b)), trusts for handicapped persons, trusts for unique and difficult situations such as drug-addicted children, and even trusts for pets.

These are just a few of the weapons in the estate-planning arsenal. If trusts sound appealing, be sure to consult the attorneys at Price & Farrington, PLLC to help you determine whether trust planning is appropriate for you.

FAMILY LIMITED PARTNERSHIPS

Despite attacks by the IRS, these partnerships are thriving as an estate-planning tool.

They certainly aren't new; they have long been popular as a technique for small business owners to protect assets from creditors. Lately, though, limited partnerships are being used for many other purposes, including even minimizing taxes on a family's investment portfolio.

In a typical arrangement, the owner of a small business or a large investment portfolio hands over those assets to a limited partnership. That person retains an ownership stake and is the general partner, remaining in charge of key decisions. The rest of the shares--limited partnership stakes--can be given away to other family or friends.

Those stakes typically are valued at sizable discounts from the market value of the underlying

assets, since they don't give the owners the clout that the general partner has. How big a discount is more of an art than a science, but discounts of 25% to 30% are fairly common. Under some circumstances much larger discounts can be justified. Often, gifts of those stakes are made gradually to take advantage of the gift-tax rules allowing tax-free gifts of $11,000 a year per person.

Limited partnerships aren't for everyone. Indeed, some tax experts warn that these partnerships often are more trouble than they are worth. They can be costly to set up and run, since they require sophisticated legal and accounting advice and appraisal costs. You also greatly increase your chances of having to explain all the details to suspicious IRS auditors. The IRS can and does challenge what it considers to be abuses, such as overly aggressive valuation discounts taken by taxpayers. *The bottom line is this: If these powerful entities are established with professional help to achieve legitimate estate planning goals, the costs associated with their maintenance are more than justified.*

BE PREPARED FOR THE IRS

Even though the IRS audits only about 1% of all individual income-tax returns, it typically picks on many more estate-tax returns, mainly because there's much more money at stake.

So make sure your tax attorney or C.P.A. has detailed financial information, including the past three or so years of income-tax returns, checkbooks, checks, property appraisals, insurance policies and any other documents you think might be helpful if you're challenged by IRS agents. In some cases, you might need even older records. Be sure your advisers know of any special circumstances, such as existing disputes between the IRS and the deceased person over back income-tax issues.

WHERE DO I GO FROM HERE?

We've mentioned only a few of the many techniques available in the estate planning attorney's toolbox. No estate planning tool or technique is a panacea, each has costs or downsides, and none should be used in a vacuum — any more than you'd expect a doctor to prescribe pills over the phone to a patient he or she has never met.

Insist that your advisors create a plan which (1) measures your needs and objectives, (2) establishes an order of needs and objectives and, most of all, (3) gives priority to those needs and objectives you feel are most important.

You probably have lots of questions at this point, including "Where do I go for competent advice?"

A good place to start is by contacting the attorneys at Price & Farrington, PLLC at 425.451.3583. But don't stop there. Educate yourself — and those you love — about the basics of estate planning. We hope this material is a good beginning.