INSIGHT ON ESTATE PLANNING

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ESTATE PLANNING PITFALL
You're using an online form to draft your will

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Time passages

Estate planning through the years

Virtually everyone needs an estate plan, but this isn't a one-size-fits-all proposition. Even though each person's situation is unique, general guidelines can be drawn depending on your current stage of life.

The early years

If you've recently embarked on a career, gotten married, or both, now is the time to build the foundation for your estate plan. And, if you've recently started a family, estate planning is even more critical.

Your will is at the forefront. Essentially, this document divides up your accumulated wealth upon death by deciding who gets what, where, when and how. With a basic will, you may, for instance, leave all your possessions to your spouse. If you have children, you might bequeath some assets to them through a trust managed by a designated party. Try to think beyond just the next few years.

A will also designates the guardian of your children if you and your spouse should die prematurely. Make sure to include a successor in case your first choice is unable to meet the responsibilities.

If you don't have a will, state law governs the disposition of assets and a court will appoint a guardian for your minor children. Most likely, you don't want these decisions taken out of your hands.

During your early years, your will may be supplemented by other documents, including trusts, if it makes sense personally. In addition, you may have a durable power of attorney that authorizes someone to manage your financial affairs if you're incapacitated. Frequently, the agent will be your spouse. Also, obtain insurance protection appropriate for your lifestyle.

The middle years

If you're a middle-aged parent, your main financial goals might be to acquire a home, or perhaps a larger home, and to set aside enough money to cover retirement goals and put your children through college. So you should modify your existing estate planning documents to meet your changing needs.

The business side of things

If you're a business owner (or hold substantial business interests), it's critical to account for the business in your estate plan. First, consider what would happen to the business if you should suddenly die or become incapacitated. Adopt contingency plans and acquire adequate insurance for these purposes.

During your middle years, begin thinking about a succession plan. Do you envision your children taking over the reins? Develop a strategy for a smooth transition.

When you're ready to retire, put your succession plan into action. Otherwise, make preparations for the sale of the business. This should be incorporated into your overall estate plan.

For instance, if you have a will in place, you should periodically review and revise it to reflect your current circumstances. Now that your children are older, you may not have to worry about a guardian, but you might shift the division of assets to accommodate college expenses. Again, a trust may be a convenient way to address these issues, especially if you're concerned about a child squandering his or her inheritance.

Typically, minor revisions to a will can be achieved through a codicil. If significant changes are required, your attorney can rewrite the will entirely.

If you haven't already created a power of attorney, the need is often more pronounced during the middle years. Furthermore, health care directives can complement a power of attorney. Reconsider the party named as your agent — frequently, the agent may change from a spouse to a younger family member or professional at this stage of life.

If you and your spouse decide to divorce, it's critical to review and revise your estate plan to avoid unwanted outcomes.

As you approach the later years, your children may have graduated from college and moved out of the house. This usually changes the dynamic for "empty nesters." Significantly, you may start shifting your emphasis from college savings to asset preservation, with appropriate revisions to estate planning documents.

The later years

Once you've reached retirement, you can usually relax somewhat, assuming you're in good financial shape. But that doesn't mean estate planning ends. It's just time for the next chapter.

For instance, you may be inclined to change bequests in your will, perhaps adding provisions to include grandchildren born in recent years. Or, if there's been a family conflict, you may wish to "disinherit" family members by removing them from your will. Depending on the situation, a codicil may suffice. Proceed cautiously, though, to ensure that you minimize or eliminate any potential challenges by the party or parties being excluded.

The same principles apply to a power of attorney. It may be advisable to designate a different agent or name a new successor. Again, a divorce can also precipitate amendments to your estate plan.

If you haven't already done so, have your attorney draft a living will to complement a health care power of attorney. This document provides guidance in life-ending situations and can ease the stress for loved ones.

Finally, create or fine-tune, if you already have one written, a letter of instructions. Although not legally binding, it can provide an inventory of assets and offer directions concerning your financial affairs.

Revisit your plan periodically

Regardless of the stage of life you're currently in, it's important to bear in mind that your estate plan isn't a static document. You and your estate planning advisor must periodically — particularly after a major life event — review and revise your plan as needed. •

Basis consistency rules come into play when inheriting property

If you're in line to inherit property from a parent or other loved one, it's critical to understand the basis consistency rules. Tax law provides that the income tax basis of property received from a deceased person cannot exceed the property's fair market value (FMV) as finally determined for estate tax purposes.

Current law

The current tax law regarding the basis consistency rules, passed in 2015, prohibits beneficiaries from arguing, as they did with some success in the past, that the estate undervalued the property and, therefore, they're entitled to claim a higher basis for income tax purposes. The higher the basis, the lower the gain on any subsequent sale of the property.

The law also requires estates to furnish information about the value of such property to the IRS and the person who inherits it.

Prior law

Under prior law, estates and their beneficiaries had conflicting incentives when it came to the valuation of a deceased person's property. Executors had an incentive to value property as low as possible to minimize estate taxes, while beneficiaries had an incentive to value property as high as possible to minimize capital gains, should they sell the property.

Generally, under Internal Revenue Code Section 1014, the basis of property received from the deceased is equal to its FMV on the date of his or her death. The property's value for estate tax purposes is deemed to be its FMV for inheritance purposes. However, in the past, beneficiaries could sometimes rebut this presumption with clear and convincing evidence that the estate had undervalued the property (provided they weren't involved in the estate valuation).

To prevent beneficiaries from challenging a property's estate tax value, the 2015 law added Secs. 1014(f) and 6035. Sec. 1014(f) requires consistency between a property's basis reflected on an estate tax return and the basis used to calculate gain when it's sold by the person who inherits it. It provides that the basis of property in the hands of a beneficiary may not exceed its value as finally determined for estate tax purposes or, if no such determination has been made, the value reported according to Sec. 6035. That section requires estates to furnish certain information about inherited property, including "a statement identifying the value of each interest in such property as reported on such return," to the IRS and to each person acquiring an interest in the property.

An asset's value is finally determined when 1) its value is reported on a federal estate tax

return and the IRS doesn't challenge it before the limitations period expires, 2) the IRS determines its value and the executor doesn't challenge it before the limitations period expires, or 3) its value is determined according to a court order or agreement.

Estates that fail to comply with the new reporting requirements are subject to failure-to-file penalties. Beneficiaries who claim an excessive basis on their income tax returns are subject to accuracy-related penalties on any resulting understatements of tax.

Not so fast . . .

Sec. 1014(f) contains a significant exception to the basis consistency rules: These rules don't apply to property unless its inclusion in the deceased's estate increased the liability for estate taxes. So, for example, the rules don't apply if the value of the deceased's estate is less than his or her unused exemption amount. Proposed regulations clarify that, if the estate is liable for estate tax, all property included in the gross estate is subject to the basis consistency rules, unless it qualifies for the marital or charitable deduction or isn't required to be appraised.

The basis consistency rules prohibit beneficiaries from arguing that the estate undervalued the property and, therefore, they're entitled to claim a higher basis for income tax purposes.

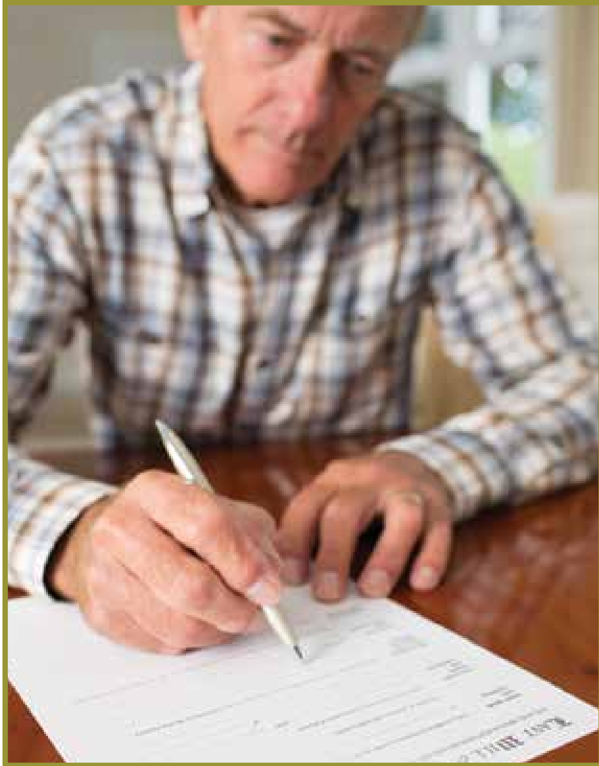
An accurate valuation is key

The basis consistency rules can be complex. The bottom line is that, if you're going to be inheriting property from a person whose estate is liable for estate tax, it's important that the property's value be accurately reported on the deceased's estate tax return. Contact us with any questions. •

Estate tax laws continue to change; so should your plan

The Tax Cuts and Jobs Act (TCJA) doubled the federal gift and estate tax exemption amount from $5 million to $10 million, adjusted annually for inflation. Combined with the unlimited marital deduction and other estate tax provisions, including portability of the exemption, a married couple can easily shelter more than $20 million from federal estate tax.

As a result, the need to incorporate estate tax planning strategies into an overall estate plan has been eliminated for everyone other than Hollywood celebrities, professional athletes and Fortune 500 CEOs — right? Wrong. Your plan should address estate tax concerns for both today and the future.



Evolution of estate tax laws

The estate tax system has undergone a radical transformation since the turn of the century. Notably, the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 featured a number of favorable changes for families.

For starters, EGTRRA gradually reduced the top estate tax rate from 55% to 35%, while simultaneously increasing the effective exemption amount from $1 million to $3.5 million. EGTRRA also provided a complete "repeal" of the federal estate tax, but only for one year — 2010. The estate tax was reinstated in 2011.

Subsequent federal tax legislation — including the American Taxpayer Relief Act (ATRA) of 2012 and the Protecting Americans from Tax Hikes (PATH) Act of 2014 — established and preserved a $5 million estate tax exemption, indexed for inflation, and a top 40% estate tax rate. Among other changes, a portability provision allowed the estate of a surviving spouse to use the remaining balance of the deceased spouse's exemption, and this provision was then made permanent.

Finally, the aforementioned TCJA doubled the $5 million exemption to $10 million, indexed for inflation. The indexed figure for 2019 is $11.40 million. Corresponding changes apply to the generation-skipping transfer tax exemption. Bear in mind that, without further legislation, the estate tax exemption will return to an inflation-adjusted $5 million in 2026.
And therein lies the rub.

Reasons for estate planning

It's clear that, during the past two decades, Congress has had no reservations about revising estate tax laws, even when certain provisions are "permanently" incorporated into the tax code. Depending on the outcome of the next few elections, lawmakers might undo some of the favorable estate tax provisions on the books or at least reduce the benefits. In that case, estate tax planning becomes more significant for a larger segment of the population.

It's clear that, during the past two decades, Congress has had no reservations about revising estate tax laws.

Furthermore, if the law is untouched, the latest increase in the gift and estate tax exemption is only temporary. It'll revert to the $5 million figure after 2025, with inflation indexing. When you consider that your assets are likely to appreciate substantially in value by then, exceeding the exemption threshold isn't as farfetched as it may seem today.

Note also that estate tax laws often differ at the state level. Despite the generous federal exemption, your family may have to contend with state estate taxes that can erode your wealth.

Finally, your personal circumstances will change over time. For example, a marriage, divorce or large inheritance will require a review of and, possibly, revisions to your estate plan.

The time for action is now

To best prepare for any future estate tax law changes, include language in your will, and your spouse's will, that provides the maximum estate tax protection for your family. Your will can be structured to take advantage of the maximum exemption available on your death.

Coordinate this with other estate planning documents, such as testamentary trusts. Your estate planning advisor can help you with the details. Remember, the estate tax laws aren't forever, so you must continue to monitor developments and adapt to any changes. •

ESTATE PLANNING PITFALL

You're using an online form to draft your will

Today, you can do practically anything online that used to require face-to-face contact. For example, you can buy clothing, do your banking or even download a form to write your own will. But a "do-it-yourself" will is a risky proposition, especially if you have considerable wealth.

Even in days of yore, some people famously drafted their own wills, often with disastrous results. A will that isn't executed properly under state law isn't legally binding. Therefore, your assets may be divided according to state intestacy laws, regardless of your intentions. And, if you have young children, a court may appoint their legal guardian.

Despite what you might read online, there's no single prototype for wills. It's complicated because the laws can vary widely from state to state. For instance, some states recognize oral wills, while others don't. Or a state may require two or even three attesting witnesses.

One common mistake of do-it-yourself wills is leaving out important provisions that can lead to challenges in the future. Case in point: If the will doesn't include a residuary clause addressing amounts that are "left over" after estate debts and tax payments have been settled, an unspecified party could walk away with a large sum of money. It might even be a family member you had wanted to "disinherit."

Bottom line: There is simply too much risk by taking shortcuts when it comes to drafting your will. Have your will drafted and executed by a reputable attorney.

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Updates on the Stokes Lawrence Trusts & Estates Team

The Stokes Lawrence Estate Planning and Administration practice was pleased to welcome three new estate planning attorneys last year. We are proud to continue our tradition of superb client service and community involvement. Below is a brief update on each of our practices:

Doug Lawrence assists high net worth individuals in evaluating and implementing personal planning strategies. He also advises individuals and professional fiduciaries on estate and trust administration matters and serves as a mediator and arbitrator in trust and estate disputes. He is active in the community, serving on the planned giving advisory board of Seattle University and on the board of directors for Heritage University.

RoseMary Reed represents clients in the areas of estate and tax planning, complex trusts, intrafamily gifts and wealth transfers, probate and trust administration, charitable planned giving, and business succession planning. She also advises nonprofit organizations on a variety of matters. She speaks regularly on trust and estate issues and recently finished her tenure as chair of the executive committee for the Real Property, Probate and Trust Section of the Washington State Bar Association.

Garon Jones focuses his practice on trusts, estates, and business succession planning for closely held businesses. He has served as the president of the Yakima Estate Planning Council and on the boards of the Yakima Valley Partners Habitat for Humanity, United Way of Central Washington, Yakima Greenway Endowment, Montessori School of Yakima, and Yakima Sunrise Rotary.

Katie Groblewski assists high net worth individuals with estate planning and trust and estate administration with a focus on families with active closely held businesses and real estate. She also counsels individual, professional and corporate fiduciaries regarding their responsibilities when serving as a Personal Representative, a Trustee or an Agent under power of attorney. Katie regularly writes and speaks on complex topics related to estate planning and administration and is an active fellow of the American College of Trust and Estate Counsel (ACTEC).

Jenna Ichikawa assists clients with all facets of the estate planning process with an emphasis on navigating complex taxable estates. She counsels families and organizations on matters such as trust and estate administration, gift and estate taxation, charitable planned giving, and laws regulating tax-exempt organizations. She serves on the board of Northwest Hope & Healing and is an active member of the Society of Trust and Estate Practitioners and Washington Women Lawyers. Jenna regularly writes and speaks on the topic of estate planning for retirement assets.

Ellen Jackson helps clients with estate planning and trust and estate administration matters, and she has a particular interest in working with owners of privately held companies. Ellen has been busy this year writing articles and giving presentations. Ellen recently served as the President of the Yakima Estate Planning Council and as a board member of the Campaign for Equal Justice. She was recently recognized as a Volunteer Attorney of the Year by Yakima Volunteer Attorney Services.

Lori Rath and Alison Warden joined the Seattle office last year. Both have established law practices that focus on estate planning, estate and trust administration, estate and gift tax, and trust and estate disputes. Lori serves on the Executive Committee of the Estate Planning Council of Seattle and is active on the professional advisory boards for several local charitable and educational institutions. Alison recently ended her term as President of QLAW Association of Washington and is the current CLE chair for the Tax Section of the Washington State Bar Association.

Saul Tilden joined the Estate Planning and Administration practice as an associate in the Yakima office last year. He assists clients with estate planning, probate and trust administration. He is a member of the Real Property, Probate and Trust Section of the Washington State Bar Association.

The lawyers in the Stokes Lawrence Estate Planning & Administration practice have been consistently recognized for their excellence by several publications and organizations, including the Chambers High Net Worth Guide, Washington Super Lawyers, and Best Lawyers in America. Many of the firm's shareholders are also Fellows in ACTEC, a distinguished national organization of estate planning attorneys in which members are elected by demonstrating the highest level of commitment to the profession, competence, experience and integrity.

If you would like to reach Garon, Ellen or Saul, please contact our Yakima office at 509-853-3000, and if you would like to reach Doug, RoseMary, Katie, Jenna, Lori or Alison, please contact our Seattle office at 206-626-6000.