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Don’t Overlook The Benefits Of Estate Planning

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Taking care of your family in the unfortunate event that something happens to you is essential in life. Having an estate plan in place can help prevent your beneficiaries from dealing with a long, contentious probate process. In addition to a comprehensive estate plan and smooth transition into the next generation, we will highlight how gifting assets while you are living can be a prudent tax move. These components of a financial plan can help provide you, your family, and beneficiaries peace of mind moving forward.

Let’s begin with the 2020 estate and gift tax exemption, which is $11.58 million a person, or $23.16 million per married couple. Assuming that these threshold amounts remain in place for the foreseeable future, the number of families who need elaborate trusts or legitimate tax loopholes is very low. Only 0.2% of Americans who die owe any estate tax. The need for permanent life insurance because of estate tax consequences is also relatively low. In the past, a family would have a life policy on a parent with the children as the beneficiaries. The beneficiaries/children would use the policy proceeds to pay the estate tax. Where it does become applicable is for families that have a vast majority of wealth tied to a business or a large farm. To sell this asset in order to pay an estate tax would be devastating for this family. They would also need to own a life policy whose premium would be a bit expensive. However, the recent increases in the exemption amount have reduced many of these cases.

For families with large amounts of wealth, annual gifting does not count against the exemption limit, and can be a useful estate planning tool. The annual gift limit is $15,000 per person in 2020. A married couple can gift split, meaning that they can each gift $15,000 to as many individuals as they want. For example, a husband and wife would be allowed to gift a total amount of $30,000 to each of their children every year. None of this counts against the exemption limit. A couple or grandparent can also front load a 529 account for five years’ worth of contributions to each child. In this example, $150,000 can be transferred. One caveat here is that the beneficiary of this 529 account cannot receive annual gifting of any type for the next 4 years.

Spending on health care and tuition also does not count against the estate tax limit. The government encourages philanthropy and non-profit endeavors. Individuals, endowments, charitable trusts, and likewise therefore help to alleviate the government’s burden. People like Warren Buffett as well as Bill and Melinda Gates have large charitable endowments that pursue such causes. This also helps by passing on a large portion of their wealth without incurring a massive estate transfer tax.

One final item to note regarding gifting. If one is gifting an asset with large appreciation, the basis for the recipient is that of the gift giver. When assets pass to the beneficiary due to a death, the beneficiary receives this asset with a stepped up basis. If the beneficiary were to sell the asset with a stepped up basis, the amount of tax owed is much less. Another reason why the tax owed is less is because the beneficiary is paying a long term capital gains, regardless of whether he/she sells the position after a day or after a year. Therefore, those who have a low cost basis or large long term capital gain should not gift them assets, instead they should let them inherit these and receive the stepped up cost basis.

Having a will, power of attorney, and a health care power of attorney is important. Many people also benefit from having a trust done by an attorney. This costs around $2,000. Trust or no trust, the important thing for most everybody to avoid is going to probate. Probate is a process that is time-consuming, costs money, and is public information. One trust to avoid is a testamentary trust, which is expensive and is also public information. Most people would not want their financial affairs to be a blurb in the local newspaper. Brokerage and retirement accounts, as well as insurance and annuity contracts, have primary and secondary beneficiary designations. These do not need to go into a will or a trust. For those who have a trust, it is necessary to fund the said trust. Naming a primary home, second home, cottage, condo, and likewise to the trust is important.

The various legal and financial minutiae of the estate process can seem overwhelming to the average person. However, with the right financial plan in place, you can ease these concerns and leave a lasting contribution to your family when you pass away. Remember to consult with an estate planning attorney and financial advisor when making these important decisions in your retirement planning process, and don't be afraid to ask questions. There are no dumb questions when it comes to your life, legacy, and family's financial security.