

FACING THE FUTURE WITH PLANNING

Estate planning is often an uncomfortable subject for many people. It is impossible to think about planning your estate without questions of death and mortality arising. Raising these issues with your spouse or children, or discussing them with an attorney can be very difficult. But the failure to do so can result in financial and emotional burdens for your family and consequences that you never intended. This outline will briefly review basic estate planning terms and concepts to help you start the process of Estate Planning.

WILLS

What is a will?

A legal document that controls the transfer of a person's property at death. In Illinois, a will must be in writing, signed by two witnesses, and made by a person who is older than 18 years of age and of sound mind.

Advantages:

- You direct who receives your property instead of your assets going to those persons that the State mandates (through intestacy laws).
- Permits you to nominate a guardian for special needs children and to create a trust for their benefit.
- You can select your executor and waive the surety on the executor's bond.
- You can give the executor power to sell assets during the probate administration.
- You can authorize the executor to continue to operate an unincorporated business.

Disadvantages:

- A will must go through the probate proceeding.
- Your assets and liabilities become a matter of public record, which can be explored by anyone.

PROBATE

What is probate?

Probate is the legal process by which the court supervises the transfer of assets from the decedent to his or her beneficiaries or heirs, either with a will (testate) or without a will (intestate).

Advantages:

- Court supervises collection of assets, payment of debts and distribution of assets.
- Creditors must file their claim against estate within six months; after that time, claims are barred.
- Independent administration is available unless heirs or legatees request supervised administration.

Disadvantages:

- Time delay, minimum period is six months before your assets can be distributed.
- Higher attorney's fees and court costs than distribution of assets through a trust.
- All assets and facts regarding your estate become a matter of public record.

Ways you can avoid probate:

- Create a living trust and transfer assets into the trust while you are alive.
- Add other persons as owners on your accounts or other assets (may cause Unintended Consequences – see discussion below).
- Have bank accounts, stocks, IRAs, and life insurance name a beneficiary on death (may cause Unintended Consequences – see discussion below).
- Make lifetime gifts (but be careful not to impoverish yourselves during lifetime).

UNINTENDED CONSEQUENCES OF POOR PLANNING

- Title to any asset which has a "named beneficiary" (life insurance, IRA, bank account or stock), automatically vests in the person named upon your death, no matter what your will or trust says about distribution of monies at your death. This may cause disproportionate distribution of your assets.
- Bank, stock or other accounts with "joint owners" are the property of all owners. Money in joint accounts can be withdrawn by *any* owner or taken by the creditors of *any* owner, even one who did not contribute any funds. A divorce or lawsuit against any owner can result in the loss of your money. Also, upon your death the joint owner becomes the sole owner of that account, despite the fact that your will or trust states that all assets are to be divided equally among all children.
- Drafting errors: If your will lacks clear language, or fails to address what happens if one of your children dies, or misnames a charitable organization, an expensive will contest could ensue.
- Questions about the capacity of ill or elderly persons to make a will or trust, or lack of proper signing or witnessing of will can result in a court ruling that the will is invalid and has no legal effect.

TRUSTS

What is a trust?

A trust is a fiduciary arrangement in which a trustee holds title to property for the benefit of a beneficiary. The grantor who creates the trust can be both the trustee and beneficiary. Trusts can be either revocable or irrevocable. A trust is intended to hold assets during one's life and after death.

Revocable "Living" Trust:

A revocable trust provides for management of your assets during your lifetime and after your death. You are the beneficiary of the trust during your lifetime. Usually you act as your own trustee until you become ill or disabled. Trusts, particularly for married couples, can be structures to avoid estate tax.

Advantages:

- As long as you are capable, you can act as trustee and retain control over your assets.
- If you become ill or disabled (and can no longer manage your financial affairs), the successor trustee steps in to manage your assets for your benefit without having a legal guardian appointed.
- You can amend or terminate a revocable trust at any time.
- There is no public record of your trust or your assets, either during your disability or after death.
- If you transfer assets to a trust, there is no probate proceeding to distribute your assets.
- You can provide protection for special beneficiaries, such as an aged parent, a minor or disabled child, or "spendthrift" or creditor protection for a person who cannot manage his or her own money.
- You direct in as much detail as you want how funds are distributed after your death (including staggered distribution over a period of time in order to avoid children receiving a large lump sum).

Disadvantages:

- Asset transfers into the trust must be completed during your life if you wish to avoid probate.

What are tax consequences?

- You continue to use your social security number to report income while you are acting as trustee.
- No separate income tax return for the trust is needed while you are living.
- You can still take the one-time capital gain exclusion on sale of principal residence.
- At death, trust assets still receive a step-up in basis to date of death values.

FEDERAL GIFT AND ESTATE TAXES

The federal and state governments impose a tax upon the gratuitous transfer of property whether made during life or at death. The gift and estate tax laws have been combined so that, for most purposes, it doesn't matter whether you give it away now or later.

GIFT TAX:

- **Annual gift tax exclusion:** Each year you may give away up to \$13,000 to an unlimited number of individuals without incurring a gift tax. A married donor can, with the consent of his or her spouse, elect to treat a gift as if it was made by both of them so \$26,000 can be gifted per person each year.
- **Direct payment:** Payments of tuition or medical bills are exempt from gift tax *if* the payments are made directly to an educational institution, doctor, or health care provider; these payments not considered gifts so the total transferred can be in excess of the \$13,000 per year.
- **Carry-over Basis:** If you transfer appreciated property as a gift, the person to whom the gift is made will use your basis in the property when that person sells the property.

FEDERAL ESTATE TAX:

Virtually all assets that a person owns at death are subject to the Federal Estate Tax. This includes real estate, stocks, bonds, bank accounts, life insurance, IRA's and company pension and profit-sharing plans. If you inherited assets from a spouse and have placed them in your name, those assets are also part of your estate, unless proper estate planning is utilized to prevent those assets from becoming a part of your estate. When you calculate your own estate value, include an estimated future appreciation of the assets. You should be aware of several important tax concepts:

- **Unlimited Marital Deduction:** If you give all your property to your spouse, there is no federal estate tax no matter the size of your estate. The Unlimited Marital Deduction also applies to the gift tax. Therefore, transfers between spouses can be made during life or at death without being subject to tax at the time of the gift or inheritance. Those assets gifted to or inherited by a spouse do, however, become a part of the estate of the spouse to whom they were gifted, and taxed at that person's death.
- **Lifetime Exemption Amount:** Each individual is entitled to a lifetime exemption amount of \$3,500,000 in 2009. Of this amount an individual may gift up to \$1,000,000 during life without gift tax. Although the exemption is quite high, many commentators believe that Congress will, in the not-too distant future, decrease the exemption amount.
- **Stepped-up Basis:** Property which is transferred at death receives a basis which is equal to the date of death value of the property. ("Stepped-up basis")
- **Charitable Gifts:** Transfers of property to a qualified charity are free of estate and gift tax – whether the transfer happens during life or upon death. There are a variety of income, gift and estate tax deductions for charitable gifts.

ILLINOIS ESTATE TAX:

Beginning in 2009, although the lifetime exemption from Federal Estate Tax is \$3,500,000, the exemption from Illinois estate tax is only \$2,000,000. Thus, an estate can be subject to Illinois estate tax while exempt from federal estate tax. Trust planning can minimize or avoid estate tax both at your death, and even upon the deaths of your children.

DISABILITY PLANNING

Property Power of Attorney:

What is a Property Power of Attorney?

A legal document which designates an agent to act on your behalf to manage your assets and financial matters.

Advantages:

- Permits management of your assets during disability
- Very flexible, can limit or expand the agent's powers as you deem appropriate.
- You can give your agent the authority to transfer assets to an already established revocable trust.
- You can give your agent the power to make gifts to named individuals.

Disadvantages:

- Under statutory form you cannot appoint co-agents.
- Not as flexible as a revocable trust during incapacity.
- Very powerful since agent has access to all of your property; possible risk of theft by your agent.

Health Care Power of Attorney:

What is a Health Care Power of Attorney?

A legal document which designates an agent to act on your behalf to make health care decisions if you are incapacitated. Illinois has a statutory form which most third parties would recognize.

Advantages:

- Very broad powers granted to an agent, for example, to admit or discharge you to a hospital, nursing home or other institution, to make all decisions regarding medical treatment. You can limit your agent's powers if you desire, in a variety of ways, on the power of attorney form.
- The agent can order the withholding of death-delaying procedures including hydration and nutrition.
- The agent has the authority to deal with post-death issues (autopsy, anatomical gift and burial).
- The statutory form contains three alternatives regarding levels of life-sustaining treatment in the event you cannot communicate. You can initial one of the alternatives which reflects your wishes.

Disadvantages:

- Under statutory form you cannot designate co-agents, although you can choose a successor agent.

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IF YOU DON'T HAVE A WILL, ILLINOIS HAS ONE FOR YOU

THE STATUTORY "WILL" OF JOHN DOE

I JOHN DOE, make this my "will", by failing to have a will of my own choice prepared by my attorney.

1. I give one-half of all my property, both personal and real estate, to my CHILDREN, and the remaining one-half to my WIFE.

2. I appoint my WIFE as Guardian of my children, if she survives me; but as a safeguard I require that:

- a. My WIFE make written account every year to Probate Court, explaining how and why she spent money necessary for proper care of our children's money;
- b. My WIFE file a performance BOND, with sureties, to be approved by Probate Court, to guarantee she will properly handle our children's money;
- c. When our children become adults, my WIFE must file a complete, itemized, written account of everything she has done with our children's money;
- d. When our son and daughter become age 18 they can do whatever they please with their shares of my estate;
- e. No one, including my WIFE, shall have the right to question how our children spend their shares.

3. If my WIFE does not survive me, or dies while any of our children are minors, I do not nominate a Guardian of our children, but hope relatives and friends may mutually agree on one, and if they cannot agree, the Probate Court can appoint any Guardian it likes, including a stranger.

4. I do not appoint an Executor of my estate, and hope the Probate Court appoints someone I would approve.

5. If my WIFE remarries, the next husband:

- a. Shall receive one-third of all my WIFE's property;
- b. Need not spend any of his share on our children, even if they need support; and
- c. Can give his share to anyone he chooses, without giving a penny to our children.

6. I do not care to learn whether there are ways to lower my death taxes, knowing as much as possible will go to the government, instead of my WIFE and our CHILDREN.

IN WITNESS WHEREOF, I have completely failed to make a different will of my own choice and the advice of my attorney, because I really did not care to go to all that bother, and I adopt this, by default, as my "will".

NO SIGNATURE REQUIRED