THE FAMILY ESTATE PLAN

WHY YOU SHOULD HAVE ONE
AND
WHAT HAPPENS IF YOU DON'T

ESTATE PLANNING

When asked about estate planning, people often respond:

> Isn't that about dying? And if so, why in the world should I be concerned? I'm young, in good health, and while we all may die from natural causes some day, that eventuality is too far off to be of any concern right now. And the chance of a freak accident is almost nonexistent. So why worry about it? Or more to the point, why spend time and money preparing for something that is so utterly remote? Is there a problem if I ignore it for now?

Of course, the answer isn't that simple. Everyone is different - each person has particular requirements influenced largely by their situation in life. Factors such as age, health, marital status, minor children (especially those with special needs), property/wealth, business interests, location, family dysfunction, etc. influence and often dictate the need to plan ahead. Also, estate planning encompasses more than where property goes when you die. It also addresses incapacity–nine times more likely before age 60–which can lead to catastrophic consequences if there is no contingency plan.

On a more positive note, an estate plan may provide significant benefits while you are alive —lower income tax, charitable giving, saving for the kid's education, and retirement. And best of all—peace of mind.

The advantages of estate planning are applicable to everyone. But the benefits go up exponentially for a young family with minor children.

SO WHAT ARE THE OPTIONS?

- You can simply to do nothing — the most popular choice.
- Or you can create a will and thereby declare in writing your wishes regarding who will manage your estate and who gets your property.
- Finally, you can create a comprehensive Family Estate Plan, which typically includes one or more living trusts[1], and numerous other documents customized to your particular situation.

Each of these alternatives or options is addressed below.

1 Where your assets (your home, bank accounts and stocks, for example) are put into the trust, administered for your benefit during your lifetime, and then transferred to your beneficiaries when you die.

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DO NOTHING

Doing nothing probably means that you:

- are not responsible for anyone (spouse, children);
- don't have any wealth (assets) to plan for;
- don't really care what happens when you are gone;
- believe death is too remote to address right now; or
- haven't given it the slightest thought.

When you die, your estate will go through probate and California law will dictate how your property will be distributed. The court will apply the state's intestacy law to give your property to your closest relatives, beginning with your spouse and children. In the absence of a spouse or children, your grandchildren or your parents will get your property. This list continues with increasingly distant relatives, including siblings, grandparents, aunts and uncles, cousins, and your spouse's relatives (yes, your in-laws). If the court exhausts this list to find that you have no living relatives by blood or marriage, the state will take your property.

Where appropriate, the court will appoint a guardian for your minor or special needs children.

If you become incapacitated and no longer able to make financial or personal decisions for yourself, the court can appoint a conservator to make these decisions for you. A court appointed conservator may also make health care and end-of-life decisions on your behalf. Feeling lucky? Maybe your court appointed agents will make the same decisions you would have made if you could. Then again, maybe not.

And a court appointed conservator or guardian can be quite expensive.

The "do nothing" approach may be appropriate if you have little or no wealth, there are no loved ones or dependents, and you are not concerned what happens if you were to become incapacitated. But if this isn't the case, its just plain silly to abrogate your responsibilities to the vagaries of a judge, outsiders, and state law.

EXECUTE A SIMPLE WILL

A will is a written legal declaration where you can:

- nominate a personal representative to manage your estate;
- designate who will, and who will not, get your property; and
- nominate a guardian for your minor children.

A will takes effect only after you die. Accordingly, it does not provide for key decisions during a period of incapacity. Like the "do nothing" approach, you may be stuck with an expensive court appointed conservator to take care of your finances and property, your personal health and medical matters, and the care and nurturing of minor children and other dependents.

A will must be submitted to a probate court for settlement. Consequently, it is a public document that anyone can access. Also, a will does not address property that passes outside of probate (see discussion below). Thus some of your property may go to people contrary to your expressed wishes as stated in your Will. And this can be frustrating to people named in your Will who may feel cheated out of their inheritance.

A will directs the personal representative to distribute your estate as quickly as practicable. It is not the best tool if you require flexibility or need to provide for the security of your family (surviving spouse, children, children from prior marriage, grandchildren) over long periods of time – maybe generations to come.

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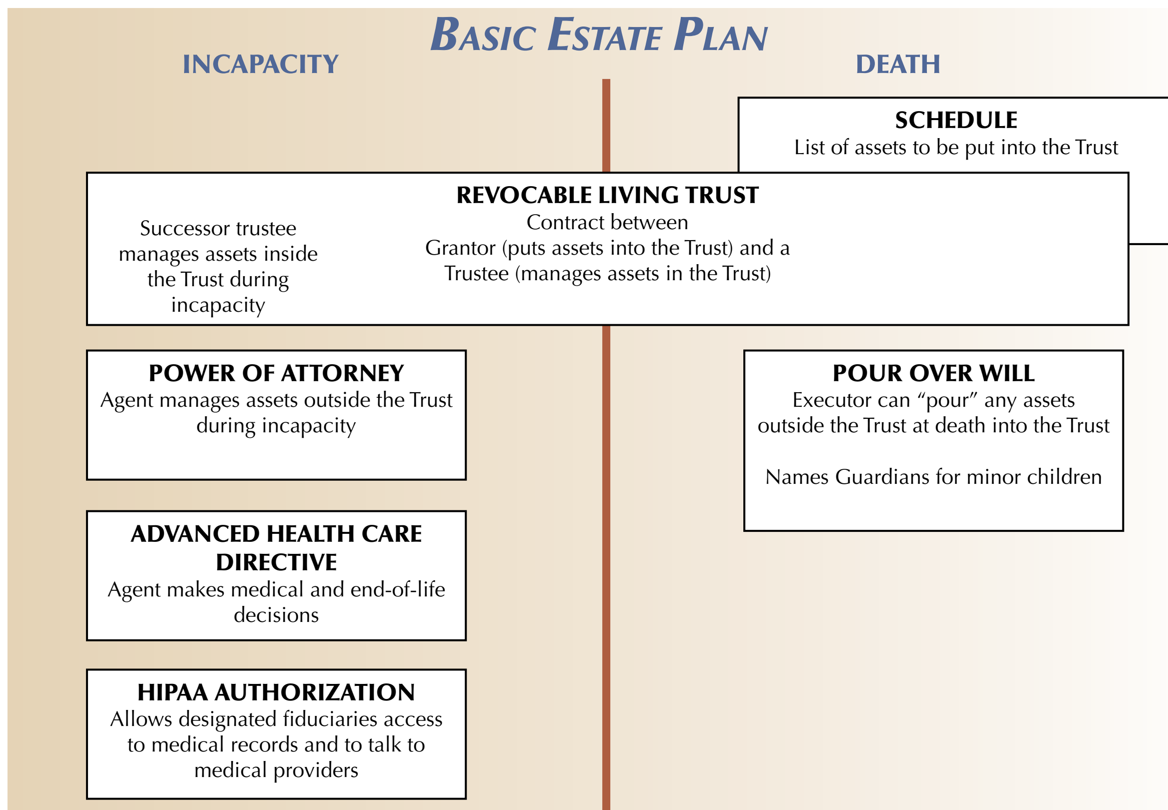
DEVELOP A FAMILY ESTATE PLAN

A family estate plan is the result of thoughtful introspection and analysis, by you and your attorney, expressed in a collection of coordinated documents. The plan is highly individualistic and should address the following goals:

- give what I have, to whom I want, the way I want, when I want;
- provide for my spouse and family;
- manage risks of sudden incapacity;
- delegate health care and end-of-life decisions (i.e., when to pull the plug);
- provide needed liquidity at death (i.e., to pay taxes, creditors);
- fulfill charitable intentions;
- promote family harmony (especially if there is a second marriage);
- plan for minor children, including children with special needs;
- lay a foundation for orderly transition of family business;
- protect assets from creditors for generations to come;
- avoid probate;
- efficient transfer of assets to heirs while minimizing:
  - probate and transfer costs;
  - taxes (income, gift, estate, property);
  - attorney, accountant, and court costs.

There is no one-size-fits-all solution. Everyone is different and having a spouse, children, other dependents, family business, out-of-state property, etc. are compelling reasons for a comprehensive estate plan. And other factors such as dysfunctional family, children with problems (drug abuse, learning disabilities or special needs), children from a prior marriage, out-of-the-country property, charitable giving, need to minimize estate taxes, etc. make estate planning a necessity.



THINGS TO CONSIDER

INCAPACITY

Incapacity is the physical or mental inability to manage one's affairs or make appropriate medical decisions on one's behalf. And this isn't that rare - a 35 year old male has a 24% chance of becoming disabled[2] for 3 months or longer during a typical lifetime. Sudden incapacity without the right agent or proxy to make business or healthcare decisions on your behalf could have serious repercussions. For example, one may want a spouse to make health care decisions but a trusted business partner to make business decisions. But maybe you're estranged from your spouse - in which case, that may be the last person you want making health care decisions for you. You can, and should, make your desires known in the proper documents.

PROBATE

Probate is a court proceeding to conclude all the legal and financial matters of the deceased. If the decedent had a will, the disposition of decedent's assets would be supervised by a probate court according to the terms of the will. Probate is a public process where court records are available to anyone for the asking. Probate can also be complex requiring not only a court appointed executor, but also an attorney and possibly a guardian for minor children. Fees for ordinary services paid to the executor and attorney are fixed by statute.[3] And Probate typically takes a year or more to conclude. The Probate Court may also name a guardian for minor children.

Is probate something inherently evil to be avoided at all costs? Certainly not. If there is a chance that heirs will challenge the will or dispute their inheritance, a court proceeding will probably be necessary to resolve the issue. Or if there is any question about the fairness or bias of the executor of the estate,[4] a probate proceeding may be the right answer since the court will provide judicial oversight over the management of the estate - thus ensuring objectivity. Finally, if the estate is small (i.e., less than $150 thousand), the estate can be distributed without probate.

NON PROBATE TRANSFERS

As mentioned above, some property can pass outside of probate. For example, the following are non-probate transfers:

- jointly owned property (e.g., real property owned as joint tenants, joint bank accounts)
- life insurance proceeds to named beneficiaries
- certain retirement accounts (IRAs, 401(k) plans)
- annuities.

Non-probate transfers happen automatically—by operation of law. To illustrate the concept, consider the following example.

David purchased property at Lake Tahoe with his savings and shared it with a college buddy named Bob. The Realtor recorded the deed as David and Bob - joint tenants. Shortly thereafter, Bob turned into a hopeless drug addict/dealer, disappeared, got caught, and did time in prison.

2 Disability is not the same as incapacity, but a significant number of disabled persons cannot make financial or medical decisions for themselves.

3 For example, on a $1 million estate statutory fees for the personal representative would be set at $23,000 and another $23,000 for an attorney - $46,000 total. Additional fees may be awarded by the court for extraordinary services (i.e., litigation).

4 This typically arises when the executor is also a beneficiary and must make decisions about estate property that could adversely affect the other heirs.

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Meanwhile, David met Mary. After a brief courtship, they got married and started a family. David created a will leaving all his property to Mary. David and Mary were deeply in love and spent a lot of time at their Lake Tahoe vacation home.

Unexpectedly, David was killed in a car accident. Mary was devastated, but looks forward to finding solace at the lake-front home she inherited.

But there is a problem. The entire Lake Tahoe property belongs to Bob since he was the joint tenant on the deed when David died. It doesn't matter that David purchased the lake house with his own money and devised it to Mary in his Will, or that Bob is still in prison. Bob is the sole and exclusive owner and may evict Mary.

And it gets worse. The fair market value of the Lake Tahoe property is included in David's gross estate and estate tax is due. Mary is the executor of David's estate, and as such, gets stuck with the tax bill while Bob gets the Tahoe house (tax free). Sound unfair? You bet it is. But it is a case-in-point of the unintended consequences of some non-probate transfers.

Similar scenarios can play out when money from life insurance, retirement plans, bank accounts, etc. go to people contrary to the decedent's clear intent as stated in a will.

Asset Protection

With small estates, its common for the executor to distribute cash (or equivalent) by simply writing a checks to the various beneficiaries. This is typically what happens with a will-based estate plan.

But what if you have significant wealth and you want to provide for your heirs over an extended period of time? Some people can handle a large cash distribution, some cannot (especially teenagers and young adults). In many cases, its important to protect those assets against predators, financial mismanagement, creditors, and divorce.

Long term asset protection requires careful planning and a sophisticated framework not available with simple will-based estate plans or the "doing nothing" approach.

Minor Children

What if the unthinkable happens - i.e., both parents are tragically killed in an accident?

Someone will be abruptly burdened with the responsibility of caring for your children and making a myriad of financial decisions regarding the property you've left behind. Will they do the right things? Make the same decisions you would - had you been alive? And how will this play out as the kids grow older?

Even parents with estate plans can still have big problems. Many estate plans make outright gifts or create for trusts on behalf of minor children with fixed distributions on designated dates, usually birthdays (e.g., 50% on the 21st birthday, and the remainder on the 30th birthday). The parent's estate is typically divided equally among all the children.

Is it a good idea to give children or young adults significant amounts of cash as lump sum distributions? Would they have the knowledge, experience, and maturity to manage the money properly? Probably not. Besides the overpowering temptation poised by the luxury car dealer down the street, unscrupulous friends and "advisors" may help them fritter away the funds in short order. As children grow up, they get involved in relationships where the partner may exert an undue influence and have designs on the inheritance. Or a child gets married - then all too often - a divorce. How do you protect money earmarked for the children from predators, creditors or a wrathful and clever ex spouse?

But there is something else wrong with this picture. Actually, several things. It doesn't take into account the unique needs or opportunities of the children at the point in time that the trust comes into being (i.e., when you die or become incapacitated). Nor does it take into account any prior investments you have made in the children. For example, you may have spent a considerable amount of money on tuition for the eldest child. Wouldn't it be fair to give the other children the same benefit? Possibly one child worked incredibly hard and got accepted at an expensive ivy league school. Would you fund that achievement even if it meant less for the other children? Or maybe a child went to a service academy (West Point, Naval Academy...) receiving an outstanding education for free. If you provided a tuition fund, does that child get nothing as a result of his/her achievement? Or what if one of your children has a developmental disability? Or special needs due to a birth defect or later in life, an accident? Or a drug or substance abuse problem? Or maybe the children have issues with creditors? The list goes on and on. Truth is, you just don't know.

Notwithstanding, the one thing you do know for sure is that your children are unique individuals who will have separate and distinct needs that will evolve over time. If you are living, you'll know how to raise your children and use your resources to their best advantage. But if you are both gone, you'll need a surrogate who will, as much as possible, fill the role as parent to your children.

The challenge is for you to establish guidelines which allow your surrogate to make future decisions and allocate funds as you would have done

had you been alive. This requires careful thought and discussion which must be incorporated in your estate plan - ***before*** the unthinkable happens.

ESTATE TAXES

When you die, your assets (real estate, bank accounts, investments, personal property, retirement plans and proceeds of life insurance) owned at the time of death are included in your "gross estate." The cost of the funeral, certain administration expenses, charitable deductions and a lifetime exemption are deducted from the gross estate to determine the taxable estate. Estate tax, due nine months after death, is 40% of the taxable estate and must be paid in cash.

The federal lifetime exemption is $5.34 million per person (in 2014). Spouses can combine their exemptions to cover a combined marital estate up to $10.68 million. In reality, relatively few couples have an estate exceeding $10 million, thus the federal estate tax is not a factor in estate planning.

But for marital estates with assets that exceed $10.68 million, the estate tax is an important consideration mandating planning and coordination between your estate planning attorney, accountant and investment advisor. This is especially true for gifts left directly to grandchildren where a special generation skipping tax can result in double taxation to the unwary.

California does not have an estate or inheritance tax.

CONCLUSION

When two people get married and start a family, they take on an immense responsibility for the care an nurturing of their children. Its hard work with unrelenting challenges through the difficult years of adolescence, college and finally into adulthood when the kids will eventually leave the nest to live independent lives.

But what if one or both parents in this family were suddenly not around? Fatal accidents, remote as they are, do happen. If you are suddenly gone, the resulting grief, uncertainty, family dysfunction, chaos, etc. would be catastrophic for your children. Each family is unique, but for most, exposing helpless children to this calamity is truly irresponsible when most of the bad effects can be easily avoided with a little planning.

You can take control and specify who and how your children will be raised and how your accumulated wealth will be used for their benefit. In the process, you can also promote family harmony and avoid costly court procedures with a carefully crafted estate plan. And the good news is the estate plan, while you are alive, can be updated as changing circumstances dictate. But if the unthinkable happens, your loved ones will be taken care of according to your wishes.

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The estate planning service I provide is my advice and counsel which manifests itself in an estate plan custom built for you. I do not sell generic fill-in-the-blank forms or one-size-fits-all products. I do not run a high-volume trust factory where you, the client, are relegated to junior staff or para-legals after a sales pitch. Rather, I spend quality time with you to understand your unique circumstances so I can craft the optimal estate plan for you and your family. I also explain your options and the operative law in layman's terms. I do this in the expectation that our relationship to be lifelong. And I fully understand the estate plan is one your family must live with after you are gone.

My approach is straight-forward and meticulous. The initial step will be a face to face meeting - not a phone call. Sometimes this happens at my office, but more often than not, I prefer to meet at your home to better understand your environment and, where appropriate, meet your family members. At the initial meeting, I will ask you a series of questions about yourselves, your objectives, your property, and any special circumstances. I will also explain the planning process in detail and what you can expect. This is an important step and allows me to understand the complexity of your situation so I can properly estimate the scope of work. And it allows you to get to know me and how I will help you. There is at no cost to you for this initial meeting.

I will draft an engagement letter outlining the work I will perform and the fees. In most circumstances, the fees will be fixed - plus out-of-pocket expenses. The amount of the fee will be based on the complexity of your case. Other factors beyond normal estate planning may require additional fees, such as out-of-state property, existence of a family business, children with special needs, charitable trusts, etc. For a married couple, a base plan starts at $2,500, but may go higher depending on the additional services required. I require an advance (retainer) of 80% of the fixed fee, which will be deposited in a trust account for your benefit.

When we start the actual engagement, I will give you a detailed questionnaire and ask you for various documents, such as bank statements, insurance contract, etc. After reviewing the detailed information, we will meet again to discuss any issues and your planning options. We will review in depth how you want your children raised, if you're not around, and the appropriate guidelines for your trustee.

I will provide you with a proposed design for your estate plan. Upon agreement of the design, I will prepare the enabling documents, give you the option of reviewing a draft of your key documents, well before any signing, and answer questions you may have. The final step will be a meeting in my office to sign the documents.

After the signing, your assets must be "funded" into the appropriate trusts. This involves retitling key ownership documents - e.g., grant deed on real property, bank account signature cards.

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TRUST CONTINUITY PROGRAM

Over time, your circumstances will change—you buy a home, the kids grow up, you start a family business, tax law changes, change jobs, health issues, win the lottery… Lots of things can happen. Accordingly, clients may sign up for an annual *Trust Continuity Program* which includes the following services:

- Update on the tax laws and any other significant legislation or cases affecting your estate plan;
- Review of your funding program and funding new assets into your trust;
- Review of your personal property memorandum;
- Annual Plan Review Letter and meeting to review your plan;
- Simple amendments to you plan documents;
- Review and update of your health care documents stored in the cloud; and
- Review and update your Durable Power of Attorney.