

Estate Planning for Penn Faculty: Getting it Right

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Estate Planning– In General

- **Estate lawyer's role-** counsellor, not mere scrivener
- **Planning for incapacity**
 - General Powers of Attorney
 - Health Care Powers of Attorney and Living Will
- **Planning for death - not just about drafting a Will or Trust**
 - **Taxes** – Estate/Gift/GST, Inheritance, Income
 - **Asset titling and Beneficiary Designations**
 - **Being thoughtful and organized** – checklist
 - **Intangibles** – legacy, “fairness”, family dynamics, control

Planning for Incapacity

- If you do not plan in advance for your own incapacity, the courts, through the state's guardianship system, will do it for you
- Guardianship is intrusive, expensive, paternalistic
- **Goal: AVOID GUARDIANSHIP! How?**

Planning for Incapacity

- Durable General Power of Attorney – designates an agent to manage financial affairs, and delineates the agent’s powers. (Springing vs. Non-Springing)
- Health Care Power of Attorney – designates agent to manage personal and medical decision making
- Living Will (can be separate, but often included as a separate section of your Health Care Power of Attorney) – to state your end of life wishes

Estate Planning Non-Tax Concepts— How Assets Pass at Death

Different ways assets can pass at death

- Probate Assets (pass under Will or if no Will, state intestacy law)
 - Outright “in own name” ownership – passes under Will
- vs. Non-Probate Assets (pass outside Will)
 - Jointly titled assets (“wros”; “entireties”)
 - “In trust for” or “TOD” or “POD” accounts
 - Beneficiary Designated (retirement accts, life ins)
 - Existing trust ownership: Trusts created by you, for your own benefit (e.g., Revocable Living Trust) and/or others; trusts created by another for your benefit
- Important note: “Non-Probate” does NOT mean it is not subject to death tax

Estate Planning Non-Tax Concepts–

Will vs. Revocable Trusts

- Sometimes referred to as “Living Trusts”
- Not for tax minimization purposes
- Not an irrevocable gift – a revocable trust is for creator’s benefit and may be changed or revoked at any time.
- Not a distribution concept – an estate plan can be implemented using either.
- Use of revocable trusts varies greatly state by state.
- A will is probated after death – filed with the local Register of Wills. In some states, probate is a bureaucratic slog. In others, it isn’t.
- A revocable trust is not probated after death.
- To be fully effective, a revocable trust needs to be funded during life. Always have a backup “pour over” will.

Estate Planning Non-Tax Concepts – Other Special Considerations

- **Blended family** - children from prior relationships, children together?
- Leaving assets **outright versus in trust** for beneficiaries: spouse, children
- **Special needs** beneficiaries
- **“Equality”**
- **Family dynamics**
- **Fiduciaries** – Who will be in charge?
 - Executors, Trustees, Guardians

Estate Planning Concepts - Outright or In Trust for Beneficiary

Some reasons for trusts:

1. Goal to provide for spouse during life – but then to children
2. Beneficiary who can't manage money
3. Creditor and quasi prenuptial planning for trust beneficiaries
4. Tax minimization for beneficiary
5. Trusts can be created to be more or less flexible and give the beneficiaries more or less control over the administration

HOW DO TAXES PLAY A ROLE?

Federal Estate Tax, Gift Tax, and Generation-Skipping Tax

Federal Estate Tax

- Single exemption of \$12.92 million (as of 2023) – estate and gift tax are “unified” – to use on gifts during lifetime and/or at death
- The 2017 Tax Act significantly increased exemption amount, **but has a sunset provision at the end of 2025 (exemption will revert to approximately ½ - \$6 million+)**
- 40% tax rate
- Unlimited marital/charitable deduction
- Portability vs. credit shelter trust

HOW DO TAXES PLAY A ROLE?

Federal Gift Tax:

- Annual exclusion (\$17,000 for 2023)
- Special rule for gifts to 529 accounts
- Direct gifts of medical or tuition excluded in any amount
- Must file gift tax return (Form 709) to document use of lifetime exemption if a taxable gift exceeds annual exclusion

Federal Generation-Skipping Tax

- Separate 40% tax on transfers to “skip persons” in excess of exemption amount
- No portability, so risk of wasting GST exemption at first spouse’s death
- Benefits of “dynasty” or generation-skipping trusts

HOW DO TAXES PLAY A ROLE?

State Death Taxes

- Some states have a death tax; some don't
- Decedent's state of residence (not beneficiary's) at death has right to tax decedent's assets, other than real estate located in another state
- Pennsylvania Inheritance Tax
 - 0% spouse, charities, child under 21
 - 4.5% lineal descendants, ancestors
 - 12% siblings
 - 15% everyone else
 - No inheritance tax on life insurance proceeds
 - PA has no gift tax – but gifts within a year of death are included

Retirement Assets Have Special Considerations

- Built-in income tax does not “go away” at death. Beneficiary will have to pay it.
- Can be subject to death taxes AND income tax
- Goal often for beneficiary to defer income tax for the longest possible period. However, effective 1/1/2020, law changes under the SECURE Act limited options for income tax deferral upon death -generally:
 - Spouse/disabled beneficiary- life expectancy.
 - All others – 10 years.
- Need careful coordination of beneficiary designations & estate plan

Retirement Assets Have Special Considerations

- Consider making **charitable gifts** from retirement accounts on beneficiary designation (tax minimization).
- Special considerations when making a trust a beneficiary of retirement assets

Retirement Assets – Penn's Plans

1. Basic Plan (401(a) plan)
2. Matching Plan (403(b) plan)
3. Supplemental Retirement Annuity Plan (403(b) plan)

* Must prepare and file separate beneficiary designation forms for each plan.

Top Mistakes Affecting Estate Plans

1. **Improper Titling of Assets or Beneficiary Designations:**
 - Unintended disposition – wrong beneficiary; outright versus in trust
 - Unintended income tax consequences for retirement account beneficiaries
 - Complicating process of administration – e.g., minor beneficiary -court appointed guardian required to access funds
2. **Failure to save first spouse-to-die's federal estate tax exemption for use by surviving spouse** – timely file federal estate tax return in first spouse's estate.
3. **Failure to make charitable bequests out of tax-deferred retirement accounts (IRAs, etc)**
4. **Blended families - unintended consequences from improper planning**

Top Mistakes Affecting Estate Plans

4. **Gifting low basis assets during lifetime** (e.g., the house or vacation home)– losing step up in cost basis at death

5. **Failure to plan for out of state real estate** - ancillary administration delay and expense

6. Failure to understand **special rules that can adversely affect intended plan:**

- Spousal Elective Share
- Pretermitted Spouse/Pretermitted Child statutes
- Spousal consent required for Qualified Plans

Top Mistakes Affecting Estate Plans

7. Use (or failure to use) trusts

- failure to consider benefits of trusts – once inheritance is received outright, children cannot create protection for themselves
- on the flip side, using trusts to “control from the grave”

8. Incorrect understanding of “use it or lose it” gifts of “bonus” estate/gift tax exemption before reversion in 2026

9. Improper Consideration of Fiduciaries

- Consider appointing children together
- Perceptions of “control” or competence



In conclusion...

Best to Plan!

... Carefully