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ESTATE PLANNING MEMORANDUM
SUMMARY

Welcome to The Paton Law Firm. You may have considered a Will, but there is so much more to “Estate Planning” these days.

A well-planned estate must have a valid and effective Will, Living Will, and Power of Attorney and Health Care Proxy. It should also consider tax planning, life insurance, disability insurance, long-term care insurance, asset protection, and other long-term care issues.

Finally, the title of the asset--individual, joint, POD, TOD must also be reviewed and considered.

To help you better understand these issues, I have prepared this summary. This is not intended to be exhaustive or specific to your needs. You probably will not need or want all of these techniques; however, you should make that decision with complete information.

INDIVIDUAL TECHNIQUES/ISSUES

A. **Will** - To insure, that assets are properly distributed and that your children and family are protected. This names your Executor, Guardian and Trustee (known collectively as “fiduciaries”) and should name back-up fiduciaries. (See Paragraph J, regarding divorce and your fiduciaries.)

A Will can also be a valuable tool for tax planning and Medicaid planning, using the following techniques. Note that most people do not have to plan to save Estate Taxes because the laws have changed. There is no NJ Estate Tax currently and the Federal Exemption is about \$12 million (This will change to \$5.4 million in 2027).

(i) **Bypass Trust** - For couples – Rarely used due to new tax laws, unless you have over \$20 million.

A typical Will leaves everything to the surviving spouse first and then if there is no surviving spouse, to the children. This can be short sighted and wastes an opportunity to save taxes. The Federal Limit is about \$12 million now, so most people don’t have to consider this.

If you move to another state you may need this. If this is a concern, my documents would allow the maximum flexibility so that the surviving spouse can make the ultimate decision when he/she has the specific facts at hand, financial condition of the couple and the then current law.

- (ii) **Disclaimers** - Valuable for post mortem tax planning and to resolve the question of whether to leave money directly to grandchildren. We can set it up so that you leave assets equally to your children. Your children can then decide to “disclaim” part or all of his/her inheritance so that the money will then go into a Trust for his/her children and he/she will be Trustee. This can have a tremendous Estate Tax savings. However, it must be established in your Will to be available after your death.
- (iii) **Medicaid Planning** - Your Will should not make bequests to a Medicaid recipient, current or potential. Any such bequest will only benefit Medicaid. Alternatively, we can add a Special Needs Trust to provide funds for Medicaid recipient, but not disqualify him/her from Medicaid.

Note that if you do not have a Will, your parents may inherit your assets under the laws of intestacy. Your parents may be receiving or applying for Medicaid benefits. This is not recommended.

- B. **Living Will** - To ensure that life support is provided or withheld according to your wishes. This is an advance directive by which you can indicate your preference for medical treatment if you cannot advise the doctors. You can refuse treatment or require maximum treatment. A Living Will can help save your family from unnecessary turmoil during tragic times. It can name a health care representative to act on your behalf or other trusted individual.
- C. **Power of Attorney** - To avoid necessity of guardianship/conservatorship and permit your spouse, child or other trusted individual access to assets and the right to make decisions for your finances, health and living arrangements. A Power of Attorney is a legal document in which you grant a trusted individual authority to act on your behalf. This can become effective immediately (Durable). Note that there is a Power of Attorney that only becomes valid in the event that you become incapacitated by an accident or are otherwise unable to handle your affairs (Springing). We do not recommend this.

Note that many financial institutions will be so restrictive in interpreting a Springing Power of Attorney that it may be too difficult to use. Further, financial institutions often do not recognize joint agents. We can prepare for this and still enforce your wishes.

- D. **Insurance Products** - To provide necessary funds for costs of illness, taxes and/or inheritance. (You will need to work with an Insurance Agent, but these products are important for a well-planned Estate.)

- (i) **Life Insurance** - To provide finances to support your family or pay taxes after your death. Note that life insurance should be owned by an Irrevocable Life Insurance Trust (“ILIT”) to save taxes, protect family members and provide for distribution.
 - (ii) **Second-to-Die Life Insurance** - A special type of policy designed to provide funds to pay Federal Estate Taxes after both spouses die. It is typically more affordable than single life insurance.
 - (iii) **First-to-Die Life Insurance** - A special policy designed to provide funds when a business partner dies and the surviving partner must buy out the decedent partner’s share in the business.
 - (iv) **Long Term Care Insurance** - This provides funds for an aide in the home or for a facility if the need arises. This is more and more important to provide care and flexibility as Medicaid reform makes it more difficult to qualify for Medicaid and as long-term care facilities expect a resident to pay privately for some period of time. If you own a business you can make the premiums tax deductible. In general, premiums can be deducted on income taxes on a limited basis.
 - (v) **VA Benefits Planning**- This can be valuable for a Veteran, his/her spouse, his/her widow/widower. There are different programs available to a Veteran or a Veteran who served during a war—even 1 day and even if he/she was not at battle.
- E. **Trusts** - to insure, that assets are properly distributed; to minimize Federal Estates taxes; to preserve estate assets in the event of a catastrophic illness. There are different types of Trusts for different purposes. For example:
- (i) **Living Irrevocable Trust** - In order to save taxes or protect from Medicaid, a Trust must be Irrevocable. This means that you can not change the terms of the Trust and you could not take back any assets that you have given to the Trust. This is an uncomfortable feeling; however, when used properly, this can save significant Federal Estate Taxes. The terms of the Trust can be very flexible and you can provide much protection for your loved ones.
 - (ii) **Living Revocable Trust** is valuable for avoiding probate in another state. You may have a vacation home in New York or Florida. These are difficult probate states. (Note that New Jersey is a very good probate state, so I do not recommend a Living Trust to avoid probate in New Jersey.)
 - (iii) **Irrevocable Living Insurance Trusts (“ILIT”)** - Very technical; but saves significant taxes – This is a living Irrevocable Trust with a twist. Instead of

putting a house, or cash, or stock, in this Trust, you add a life insurance policy. Life insurance is taxable for Federal Estate Taxes. It is not taxable for income taxes. Thus, there is much confusion about the taxability of life insurance. There are certain administrative rules that must be followed, but when done properly, life insurance Trusts save significant taxes. It also protects your family and provides for distribution rules.

- (iv) **Testamentary Trust** - A Testamentary Trust is set forth in your Will. It can be used for many reasons, including tax savings, protecting a spend thrift or minor child, protecting assets from Medicaid. However, you do not have to fund this Trust until you die. We do have to specify the terms of the Trust in your Will.

- F. **Lifetime Gifts** - To minimize Federal Estate taxes. Note that most people do not have to be concerned about this limit due to the increase in the Federal Gift and Estate Tax Exemption. However, when appropriate, this gifting can be used to get significant amounts of money out of your Estate tax free.

Every person is allowed to gift \$16,000.00 to any person they choose. A couple can gift \$32,000.00 annually to each person. This could be family members, friends and neighbors.

Note further that you can also pay for a person's medical and/or educational expenses without incurring gift taxes provided payment is made directly to the provider. This is another way to get significant assets out of your estate. Do not confuse the fact that you can make these gifts under tax laws to mean that we can gift for Medicaid.

Note finally, Medicaid does not allow any gifting in the 5 years before applying for Medicaid regardless of the Gift Tax Laws. (See H below)

- G. **Charitable Remainder Trust** - Charitable Gifting can be used to benefit a charity and to protect your family. A Charitable Remainder Trust is a wonderful tool to save taxes and still protect your family. You can take appreciated stock and contribute to a Charitable Remainder Trust. This Trust could require that you receive an income stream from the Trust for the rest of your life and your spouse's life. When you die the stock will go to charity. You can choose the amount of income received annually. This can be an extremely beneficial tool for you because it converts an illiquid asset to a cash stream.

Typically, the stock has appreciated so much that if you sell it, you will have to pay significant Federal capital gains taxes. Many times, the stock does not pay a dividend. Using this tool, you have created an income stream, received a current income tax deduction and provided for a worthy charity. Further, you avoided Federal Estate Taxes on the stock. If you combine this with a life insurance policy in an Irrevocable Life Insurance Trust, you can replace the value of the asset to your family at a nominal cost.

- H. **Gifts/Medicaid** - As you probably know, Medicaid has increased the look back period from three years to five years. Additionally, it now allows for any and all gifts to be accumulated and totaled. (It used to be that Medicaid would only look for significant gifts of approximately \$1,000.00 at a time.) Further, the disqualification period now runs from the date you apply for Medicaid; not the date of the gift.

Medicaid currently does not exclude charitable gifts made during the five year look back period. Unfortunately, when implemented literally, the \$20.00/week that you donate to your Church or Temple, could have a detrimental affect on a Medicaid application. It is too early to know how Medicaid will actually deal with such charitable gifting. However, under current rules, you would have to go to a “fair hearing” and explain the gifting.

Note that, even though the Tax laws allow gifting; Medicaid does not.

- I. **Business Succession Planning** - If you are a business owner, your business is a significant asset. It is very likely that your death or disability will seriously affect the value of your business. Therefore, you should have a plan in place to protect your business.

Alternatively, you may want to retire some day. You may have some family in the business and others that are not in the business. We can prepare plans to protect your business and family.

We can also use your business ownership in your personal planning since your business can pay for long-term care insurance with before tax dollars.

- J. **Divorce, as it affects your Estate Planning Documents** - The new probate law states that if you are divorced and do not update your estate planning documents, (including your Will, Living Will, Power of Attorney, Trusts, Guardians for your children, etc.) then your documents will automatically be interpreted to remove your ex-spouse and any of your in laws to whom you are related because of your ex-spouse. This sounds right, but there are broader issues.

Suppose you named your brother-in-law as Trustee for your children because he is a financial wiz, good guy and uncle to your children. You trust him. You maintain an independent relationship with him after the divorce. You still want him to be Trustee for your children. Not so. You have to update your Will/Trust to make that happen.

- K. **Ownership of Assets** - The way that you own an asset can affect how it is distributed at your death. If you own an asset jointly with another person with a right of survivorship, or you name a beneficiary on your IRA, life insurance policy, stock account, etc., then the named beneficiary or joint owner will receive the asset regardless of what your Will provides. If you own it jointly without a right of survivorship, then your Will controls only your interest in the asset. We need to review your assets, ownership and goals to plan properly.

Obviously, not every estate requires all of these devices and certain strategies are not practical for every estate. You must prioritize your goals in order to properly plan your estate. I can help you review your goals and determine the best plan for your needs.

Please feel free to call and discuss your personal situation and goals.

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