Estate Planning for Every Stage of Life

SACHETTA
For Life's Road Ahead

Estate Planning for Every Stage of Life

Wealth Management is mainly about protecting your assets and loved ones. Estate planning (a subset of Wealth Management) allows you to extend those protections beyond your own lifespan by passing down what you've earned to the next generation with minimal taxation and complications. Estate planning also allows you to control what happens to you if you cannot make your own medical and financial decisions someday.

No matter your age or wealth, estate planning is a critically important part of comprehensive Wealth Management. Estate planning advisors work with clients at all stages of life to develop strategies to put their minds at ease.

You've spent years working and strategizing with your financial advisors to grow your wealth. Estate planning will help transfer that benefit to the next generation.

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State and Federal Estate Tax Laws: A Basic Overview

Estate planning isn't something any of us can afford to put off, as the future is entirely unpredictable. If something happened to you today, would your family have the resources to take care of themselves? Would all your assets pass to your loved ones? How much of your money would go toward paying estate taxes instead of to your heirs? Would all your final wishes be respected?

Who Pays Estate Taxes?

A person's estate may owe estate taxes after they die, depending on their Net Worth, since both federal and some state governments can impose estate taxes if the total fair market value of the decedent's taxable property exceeds a certain amount.

Estate taxes must be paid out of the decedent's estate before assets are distributed to their heirs. The decedent's personal representative/executor is responsible for remitting any taxes owed. With estate tax rates as high as 40 percent, taxable estates lose much of their value before heirs get anything.

Federal Law and Estate Tax Exclusions

The federal estate tax exclusion is high enough that most American families will never pay federal estate taxes. Right now, these taxes are only relevant for the very wealthy—though many more families will be affected starting in 2026 (absent any future legislative changes).

The IRS uses the basic exclusion amount (BEA) to determine an individual's federal estate tax obligation. The BEA is increased each year to adjust for inflation. For 2022, the federal estate tax exclusion amount is $12.06 million per individual. Married couples may combine their individual exclusion amounts to shield joint assets. In other words, if wealthy spouses both die in 2022, their estates can avoid estate taxes on a total of $24.12M in assets.

Many more estates are expected to incur federal estate taxes in the near future. That's because the federal exclusion amount more than doubled when the Tax Cuts and Jobs Act took effect in 2018, and is set to revert to its pre-TCJA level starting in 2026. It's unknown precisely what the new BEA will be at that time since it is dependent on inflation adjustments, but will likely fall somewhere in the low $6 million range per person.

State Laws and Estate Taxes

In addition to the federal government, 12 states and Washington D.C. also levy estate taxes on the estates of their residents. The states are

> Connecticut, Hawaii, Illinois, Maine, Maryland, Massachusetts, Minnesota, New York, Oregon, Rhode Island, Vermont, and Washington.

Each state's estate tax laws are unique, but all the states use exclusion thresholds much lower than the federal amount. Massachusetts and Oregon have the lowest thresholds at just $1 million per individual. This means that many estates owe state taxes, but not federal.

Residents in these places must be extra diligent about estate planning to protect their assets. For example, take a retired Massachusetts resident who has modest assets and has owned a home in a Boston suburb for 30 years. The property is valued at $2M now. If they die with the home in their own name and their estate is worth $2.5M, the estate will have to pay Massachusetts estate taxes (with a maximum tax rate of 40 percent) on the entire amount.

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The same resident could use estate planning strategies like trusts to remove the property from their taxable estate without necessarily leaving or selling their home. The fair market value of their estate is just $500,000 when they die, so no estate taxes are owed. Their heirs could split up that money plus inherit the property from the trust where their parent held it.

Gifting and Estate Taxes

Gifting may be part of your estate planning strategy for several tax-advantaged reasons. Giving away property and assets reduces the size of your taxable estate, so it can be done as part of MassHealth planning or as a strategy to lower or avoid estate taxes.

Gifting can also have tax consequences for the giver. Any gifts you make that exceed the IRS's annual gift tax exclusion amount ($16,000 per recipient for 2022) are subject to the gift tax. The person who gives the gifts is responsible for the tax, which ranges from 18 to 40 percent. Gift taxes can be avoided, but only in certain circumstances. For example, paying for someone's tuition or medical costs isn't considered a taxable gift, provided the payments are made directly to the education or medical provider. Gifts to a spouse, political organization, or charitable organization may also be exempt from gift taxes.

Anyone who makes significant, taxable gifts during their lifetime should be aware that the IRS adds those gifts back into the value of your estate when determining whether it owes estate taxes. Say someone gives away $3M to younger relatives during their lifetime and dies in 2022 with an estate valued at $10M. The $3M in taxable gifts is added for a total taxable estate of $13M, exceeding the 2022 lifetime exclusion of $12.06M.

This decedent's lifetime gifts would trigger federal estate taxes. This is just one example of the importance of discussing gifting strategy with advisors before writing any checks.

Trusts for Estate Planning: Different Types for Different Purposes

There's a common misconception that trusts are only for the wealthy. In reality, all kinds of people use trusts to achieve their estate planning goals. Trusts are highly customizable and can be used for many purposes. The key reasons people create trusts for estate planning include minimizing estate taxes, protecting minor children or other vulnerable family members, shielding assets from creditors and transferring assets to the next generation without going through probate.

Using Trusts for Estate Planning: How Trusts Work

While many kinds of trusts exist, there are generally three parties involved. Say you want to use a trust to transfer some money and property to your kids. You would create a written trust document stating the terms of the trust. For example, do you want the kids to receive distributions from the trust when they reach a certain age, or are there other benchmarks you want them to hit before they can receive money from the trust?

As the person creating the trust, you're the grantor/trustor. Your kids are the beneficiaries. You would also name at least one trustee in the trust document, who's responsible for overseeing and administering

the trust and its assets. Trustees may be trusted individuals or entities like your wealth manager or a private bank/trust company. They have a responsibility to manage the money in the trust and distribute it to beneficiaries in keeping with the terms you lay out in the trust document.

Basic Types of Trusts for Estate Planning

Depending on what you're trying to accomplish, your estate planning advisors might suggest creating one or more of these types of trusts:

Irrevocable trusts generally can't be changed or terminated once they're in effect. People commonly use irrevocable trusts for estate planning as a way to to minimize estate taxes. Assets that you move to an irrevocable trust no longer legally belong to you but to the trust. That means they're not counted toward your taxable estate for estate tax purposes, nor can they be seized by any creditors you may have.

Revocable trusts are also called living trusts. As the name implies, you can revoke or alter a revocable trust throughout your life. Assets that you hold in a revocable trust are still legally your property, so they're vulnerable to any creditors you may have and they'll add to your estate tax burden when you die. A revocable trust becomes irrevocable and unchangeable once the grantor dies. At that point assets can be passed to heirs outside of the probate process in accordance with the grantor's wishes. A revocable trust is typically used to avoid the public probate process and ensure your wishes are carried out privately after your death.

Special needs trusts are often used by parents and grandparents of disabled children. SNTs allow grantors to put aside money for the future care of a beneficiary with special needs. By creating this kind of irrevocable trust, you can make sure that your loved one with special needs will have a trustee overseeing their financial wellbeing if you're unable to do it. SNTs need to be established carefully to ensure that assets held in the trust are never legally the property of the beneficiary. That could affect their ability to qualify for any governmental benefits they need in the future.

Irrevocable life insurance trusts (ILIT) are a special kind of irrevocable trust that's specifically used to own the trust grantor's life insurance policy. Without such a trust, your life insurance's death benefit could be considered part of your taxable estate when you die. Payouts provided by the policy can be distributed to beneficiaries through the trust.

Generation-skipping trusts are typically used by grandparents as a way to pass assets directly to grandkids. This strategy is generally used to minimize transfer taxes. Passing assets to your children and then having them pass their inherited assets to their own children means the same assets may be taxed twice as they go through two estates. The idea with using a GST is to skip that first round of taxation. If the skipped generation is financially comfortable and doesn't need the inheritance, this strategy can work well for all parties.

Note that a generation-skipping trust doesn't have to be set up to benefit relatives. A grantor can designate anyone who is at least 37.5 years younger than themselves as a beneficiary of this kind of trust.

Charitable trusts can be used to transfer assets to charitable organizations in ways that are tax advantaged for the donor. There are even ways to structure charitable trusts so the grantor receives an income stream from the trust during their lifetime.

3 Essential Estate Planning Documents

What would happen if you were in a terrible accident today and landed in the hospital, seriously injured and unable to speak for yourself? It's the type of scenario that no one wants to think about, but it could happen to anyone. It's this uncertainty that underscores the importance for all adults to complete some basic estate planning documents.

Wills and trust documents say a lot about what you want to happen to your assets after you die, so people might not get around to creating them until they have some money and/or dependents. But the following estate planning documents are highly recommended for anyone over 18-year-olds, regardless of wealth.

Health Care Proxy

A health care proxy is a simple form that allows you to name someone to make medical decisions on your behalf, if you're incapacitated. In cases of serious injury or illness, your doctors should ask your proxy ("Agent") to decide whether to try a particular kind of treatment. A health care proxy form should also ask for at least one alternate person who can act as Agent if the first person named isn't available. Choose people familiar with your wishes around life support since they can accept or refuse life-saving treatment on your behalf.

A health care proxy form also states your wishes for organ donation.

Power of Attorney

A power of attorney is used to name someone (your "attorney-in-fact") to handle your financial business if you are unable. Your attorney-in-fact can do things like accessing your accounts to pay your bills and communicate with the IRS on your behalf. People often complete a power of attorney when they're in the military and preparing to serve abroad. Still, you could also need one on file if you're unexpectedly incapacitated.

HIPAA Authorization

A HIPAA authorization form isn't something that everyone has as part of their estate plan. It's extra protection in case you're hurt or sick and want your doctors to be free to share medical information with your loved ones.

This form serves a slightly different purpose than your health care proxy. The proxy form authorizes your Agent to receive information about your condition if you cannot speak for yourself. A HIPAA authorization form has a broader scope. You can permit healthcare organizations to disclose some or all of your medical information to one or more people, not just the person you're trusting to make decisions. This makes it easier for everyone to stay in the loop if you're ever incapacitated.

Advance Care Directive/Living Will

It's common to hear people use the terms advance care directive, personal directive, and living will interchangeably. These forms are where you can share your wishes about many elements of end-of-life care and life-sustaining care. Your living will is highly customizable, so you can share as much information as you want about any views, beliefs, and requests that may be relevant if you're incapacitated. Your doctors have no legal requirement to follow what you request. But your living will may help guide them and your Agent to make the decisions you would want them to make.

Final Thoughts on Estate Planning Documents

Unlike wills and trusts, these basic estate planning documents are simple to create. You probably don't need to consult an attorney or other advisors. Just write down everything you want to write, have forms notarized if necessary and hand out copies to anyone who might need to know about your documents. States have created their own printable estate planning document templates to make this easy. (That said, you can always talk to your estate planning advisors about any document questions that come up.)

Revisit your estate planning documents annually to ensure that your written wishes still reflect what you want. Update forms whenever circumstances change with someone you've named as an agent or backup. Someone who moves out of the country or starts experiencing dementia isn't going to be an ideal health care proxy. Keep those documents updated with at least three local, trusted agents named in each one.

4 Estate Planning and Children

Estate planning and children go hand-in-hand. The birth of their first child is often the event that causes someone to call estate planning advisors for the first time. It's a weight off your shoulders to know that your young children have some financial and legal protections in place if you die or are incapacitated.

Guardianship and Money Management for Minors

For parents of minor children, estate planning documents should answer a few core questions.

- Who should take care of the kids? Use your will to name the person/couple you would want to have legal and physical custody of your kids, as well as an alternate person or couple. While the courts ultimately decide who will take custody of minor children if their parents are gone, guardianship designations in the parents' wills carry a lot of weight.
- Where will the money come from for kids' care? Parents can work with estate planning advisors to make sure that kids are financially protected in a few different ways. Buying life insurance policies and funding education savings plans like 529 plans are two ways for parents to take care of some big financial needs that kids might have in the future. Using trusts to hold and transfer assets to kids is also a standard part of estate planning for minor children.

- Who's in charge of the money? The same person who gets guardianship of the kids shouldn't necessarily be named as trustee. Parents can (and often should) have different people in charge of caring for the children and managing the money that provides for their care.

Estate Planning for Children with Disabilities

For parents, grandparents and guardians of children with disabilities, estate planning takes on extra importance. Here are just some of the considerations that might be part of the conversations parents and guardians have when discussing estate planning and children with their advisors.

A child with a disability might need ongoing financial and physical support throughout their lives. Parents or other guardians who currently provide that support must use estate planning to ensure that resources are in place to meet their child's future needs. It's an ongoing process. Plans should be adjusted as the child grows and their needs evolve.

A few things to keep in mind around estate planning and children with disabilities:

- Be careful not to transfer assets to children in a way that risks their ability to get government benefits. If they have legal control over money or other assets, they may not meet income qualifications for some of the services they need in the future.
- Parents/guardians of children with disabilities may have more substantial insurance needs than their peers. A parent who is the primary caretaker for a child with a severe disability must think about insurance to pay for skilled caretakers or long-term care when the parent is no longer able to do it.
- Think about what kind of resources and support the child with a disability would need, in addition to money, if their primary parent or guardian were suddenly incapacitated. Create a letter of intent or other documentation with information that caretakers/advocates/guardians should know about the child and best practices for their care, in case you can't convey that information in person.

Using Estate Planning to Transfer Assets to Children/Younger Generations

There are many estate planning strategies that you may use to transfer assets to children, grandchildren and other younger relatives. Many people simply leave things to their loved ones in their will, though this strategy requires the estate to complete probate before heirs can access their inherited assets. Naming kids as the beneficiaries on life insurance or retirement accounts allows them to inherit assets without going through probate.

Paying for their tuition is another generous way to support younger relatives, and payments made directly to the institution aren't subject to gift taxes. And many families use one or more kinds of trust as a way to pass assets to the next generation without incurring estate taxes.

Make sure to share not just your money but your money management wisdom too. Help the next generation develop the financial skills they need to manage inherited money and stretch it into the next generations. Talk through hypothetical money decisions and the consequences of various choices. Teach them about basic investing concepts. You can even bring them to meetings with your financial and estate planning advisors. Encourage them to ask questions about anything that's confusing.

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Estate Planning and Marriage

People often wonder how they should approach estate planning when they're married. Should both spouses go together to see their estate planning advisors or create their own separate plans? How does being married affect estate tax planning? How should you account for joint assets in estate planning?

Estate planning for married couples isn't necessarily much more complicated than a single person's estate planning. Every individual's situation and needs are unique, and your advisors can talk you through everything you need to know. Here are general answers to a few questions people typically ask about marriage and estate planning.

Should we do estate planning together?

Married couples certainly aren't required to do estate planning together or work with the same advisors, but it's a common-sense way of ensuring you're on the same page. Typically, each spouse will create their own will and complete other estate planning documents individually. Trusts can be created by you as individuals or together if you want to fund the trust with your own money.

Speak to your advisors together if you can. It ensures you both have the same information and that your estate plans aren't in conflict with one another. For example, you wouldn't want to name different

people as guardians for minor kids in your wills. Estate planning together is also cheaper than doing it separately.

How do we manage separate and joint assets?

Deciding how to title assets that you share can be a complicated part of estate planning. Each partner may want to keep certain assets in their own name. This will protect them from becoming the other spouse's property in case of divorce and can have estate planning tax advantages. Assets that you share jointly will become the sole property of the surviving spouse when the first spouse passes away.

What is portability, and why does it matter?

The concept of portability can be important for estate tax planning for married couples. The federal estate tax does allow for portability. This means that when one spouse dies, the surviving spouse can use any of their unused estate tax exclusion amount for themselves. So, if Spouse A dies in 2022 with an estate valued at $10M, they didn't use $2.06M of their estate tax exclusion. Spouse B can add that amount to their own exclusion amount and shield as much as $14.12M from estate taxes.

However, states with their own estate taxes don't necessarily have portability. The Massachusetts estate tax doesn't allow for it, which makes estate tax planning even more important for Massachusetts residents. If your spouse only uses half of their $1M estate tax exclusion, your estate still only gets to shield $1M from estate taxes.

Estate Planning After Divorce

It's always a good idea to review your estate plans after ending your marriage. Let's say you don't get around to updating your documents, and then you're seriously injured in a car accident. You probably don't want to regain consciousness to find that your ex-spouse has been making medical decisions for you while your new partner is stuck in the hospital lobby. And if you died before updating your life insurance, you probably wouldn't want your ex getting the death benefit.

There are exceptions, of course. Some former spouses maintain a close relationship after divorcing and still trust and support one another. But most people will want to revisit their estate planning documents. You may want to update your will to name a new personal representative and remove your ex as one of your heirs. Create a new health care proxy and HIPAA authorization and send copies to your healthcare providers. Update your beneficiary designations for life insurance and retirement policies.

Divorced couples who continue to co-parent naturally have additional estate planning complications to work through, especially if one or both parents remarry. Speak to your estate planning advisors about any changes to your family structure so we can adjust your existing plans to reflect your new life.

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Navigating Complex Estate Planning Decisions

Because you're making decisions about family, money, and your own unpredictable future, many complicated and touchy subjects arise during estate planning. There's no rule-of-thumb solution for most estate planning questions. Always discuss specific questions with tax and estate planning advisors to evaluate your options and find the best strategies.

That said, we hear many of the same issues come up again and again. These are examples of just some of the common (yet complex) questions people ask their estate planning advisors.

How should I transfer my house or other real estate to my heirs?

There are many ways to transfer a home to heirs using estate planning, and each has pros and cons. The estate tax, gift tax, and capital gains considerations all come up, so it's vital to run all the scenarios.

- Transferring real estate using trusts can be done in a few different ways. One option is to create a Qualified Personal Resident Trust (QPRT) to own the property. The person you intend to inherit the house is named as the beneficiary. The trust has a specific term length, during which the parent can continue living in the house.

If the parent outlives the term of the trust, the home is effectively removed from their taxable estate. The beneficiary takes ownership and may allow the parent to keep living in the home and paying rent at the fair market value. Or, the new owner can evict the parent if they want. If the parents die before the end of the term length, the trust is "unwound", and the home's value is counted toward the parent's taxable estate. In this situation, it's a nothing venture, nothing gained proposition.

- Leaving the home to kids in your will is a popular estate planning strategy. The parent continue to keep their home until the end of their life, and the heir who inherits receives a step-up in basis that should lower (or eliminate) their capital gains tax bill when they eventually sell the home. But the estate has to go through probate first.
- Gifting the house outright can have tax implications for wealthy parents. The entire value of the property that exceeds your annual gift tax exclusion amount ($16,000) is taxed, but it counts toward your lifetime estate and gift tax exclusion. Say you give away a home worth $500,000 in 2022 when the annual exclusion amount is $16,000. The remaining $484,000 is a taxable gift, but you don't have to pay gift taxes immediately. Report the gift to the IRS and count the $484,000 taxable gift toward your $12.06 million lifetime exclusion. If you don't exceed that exclusion amount, your estate won't be taxed when you die. This could become more of an issue when the lifetime exclusion drops back to pre-2018 levels in 2026, and more estates owe taxes.
- Selling the property to one or more kids can be done in several ways. The kids can buy the home at fair market value. Parents may even lend them the money to afford the purchase. Or, the parent can accept a discounted price—but the difference between the fair market value and the sale price is considered a gift for tax purposes.

How should I plan for future healthcare/long-term care costs?

A plan to pay for your future medical costs helps protect the assets you've set aside to pass down to the next generation.

There are a few ways to use estate planning to prepare for high healthcare and long-term care costs.

Transferring property out of your name now may help you qualify for long-term care coverage if you need it later. MassHealth (and Medicare programs in other states) use a five-year lookback period to determine an applicant's eligibility. There are strict rules about getting rid of assets during that period. Work with your advisors to make a plan for qualifying for MassHealth.

Your advisors can also help you determine if it makes sense to buy long-term care and/or disability insurance. The latter can help cover your expenses if you're unable to work because of a temporary disability, in which case Social Security disability benefits won't be available to you.

Advisors can help you find tax-advantaged strategies to make philanthropic gifts both during life and after your death.

What's the most tax-advantaged way to build charitable giving into my estate plan?

Estate planning can be a win-win proposition for you and your favorite charitable causes. Advisors can help you find tax-advantaged strategies to make philanthropic gifts both during life and after your death. Making gifts now can get you an income tax deduction and other benefits. For example, donating appreciated stock to charity entitles you to a tax deduction and spares you from the capital gains taxes you'd pay if you sold the stock.

Leaving some of your assets to charity when you die can also be a good tax strategy. For example, naming a charity as a beneficiary on a retirement account keeps that account from being added to your taxable estate. The organization gets a nice big donation, and your heirs might even avoid estate taxes by keeping that extra money out of the estate. (In places like Massachusetts with low estate tax thresholds, even small amounts of money can tip your estate into the taxable territory.)

What if I own my business?

Business owners have additional considerations to discuss with their estate planning advisors. What's your succession plan? Are there partners who will buy out your share of the business when you die, and how will that affect the heirs who then inherit that money? What happens to your business debt? What happens if you're a sole proprietor? What if it's a family-owned business? Estate planning for business owners is essential to protect your professional legacy and employees, as well as your family and other loved ones.

Conclusion

Estate planning can be complex, but it doesn't need to feel daunting. With experienced advisors who can guide you through the process, estate planning should make you feel more relaxed about an unpredictable future. No matter what comes next, you'll know that you've got plans in place to protect yourself and the people you love most.

Sachetta's advisors are always here to help you create the financial plans that give you and your family peace of mind. Our extensive referral network includes top estate planning advisors, making it easy for our clients to connect with the estate planning resources they need to complement their overall financial plans. Contact us today.

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