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INTRODUCTION

We are giving you this set of Estate Planning Questions and Answers to answer many of the questions that clients often have. If you take the time to read it before our meeting, then our meeting may go faster, and that may reduce your legal fees.

Why do I need an estate plan?

You may become incapacitated. Your estate plan can provide for management of your financial affairs and your medical care.

You want to protect your family on your death. Your plan can say who will control your assets. You may want to set up a Trust so that a person with financial experience can manage your assets for family members who are too young or inexperienced to handle financial matters. You may want to set up a Trust to help protect your family from creditors. You want to be sure that your family will have enough money to live on.

You want to save on death taxes. Your plan can help reduce those taxes. **The estate of a person who dies in 2021 has a $11,700,000 exemption from tax, but will be subject to a 40% tax above that level.** The exemption is scheduled to increase with changes in the cost of living. A well-drawn estate plan can help minimize death taxes for you, your spouse and your children. However, your plan shouldn't interfere with your enjoyment of your assets. If you decide to make gifts, you should balance this decision against the need to preserve your assets so that you can be comfortable and financially independent for your lifetime.

How much will my estate plan cost?

The cost depends on many factors. We charge for our estate planning services on an hourly rate basis. Our firm uses specialized computer programs so that we can be efficient. We also use paralegals when possible, to keep costs to a minimum. Finally, we do things like give you this information package and ask you to fill out the enclosed questionnaire, so that we can keep your costs down.

Generally, the more complicated the plan, the higher the cost. Fees may range from as low as $4,000 to $20,000 or more. It's hard to give you an estimate of the cost until after the first meeting, when you decide what kind of plan you want. **A typical plan for a married couple, consisting of "pour-over" Wills, a Living Trust and Powers of Attorney, might cost between $6,000 and $8,000**.

Can I make changes to my estate plan after I sign it? How much will it cost to make changes?

You can change your Will or Living Trust at any time. You should review your documents whenever there is a change in your family (such as a birth, marriage or divorce), if there are changes in the law, or in any event every five years. Changes may involve a simple amendment (costing only a few hundred dollars), or you may need an entire new plan if your circumstances change (costing as much as or more than your original plan).

Some parts of your plan may be "irrevocable" and can't be changed. For example, if you give assets away, you can't get them back. Some people want to set up trusts to fund the college education of their children or grandchildren, and these trusts usually are irrevocable.

What should I send Hoffman, Sabban & Watenmaker now?

Send us a copy of your current Will, Trusts and Powers of Attorney, if you have any. If we can read them before meeting you, the meeting will be more productive.

What should I bring to the first meeting?

A filled-out questionnaire. Please try to complete the questionnaire included in this packet before the meeting. It will give us important information and save time during our meeting (which may reduce our fees), and it will get you thinking about the kind of plan you want.

A list of your assets with their approximate values and a list of your liabilities.

A list of your life insurance and retirement plans. The list should include the amount of any life insurance, with the owner of the policy and the beneficiaries. If the policies have cash values, try to find out the amount of the cash value. If you have any pension benefits or IRA's, please try to find out the names of the beneficiaries and the amount of your benefits.

This financial information will help us to determine your family's financial position upon your death. It will allow us to estimate the estate taxes and the amount of cash available to your estate to pay taxes and expenses, and the amount that will be left for your family so we can tell whether you have too much or not enough life insurance.

Other important documents. Please bring copies of any premarital agreements, buy-sell agreements, operating agreements and partnership agreements (if you can find them), as well as grant deeds and property tax bills for your real estate.

PROBATE

What is probate?

Probate is a court supervised procedure. The Judge decides whether you have left a valid Will. The Judge also appoints an Executor (whom you can designate in your Will). The Executor makes a list of your assets, notifies creditors, pays your debts, files any required tax returns, and manages your assets during this time. When the Executor's work is done, the Judge will issue a court order transferring to your designated beneficiaries the legal title to your assets.

How long does probate last?

Probate can take up to two years for estates large enough to require the filing of an estate tax return. (For 2020, a return is required for estates with gross assets of $11,700,000.) This delay is mostly because it may take that long for the IRS to audit the estate tax return. Smaller estates may be closed in less time, but normally at least one year. The Probate Court is often backed up, and so it can take three months just to get a Will admitted to probate and have an Executor appointed.

What assets must be probated?

Generally, any assets that you own in your name alone must be probated.

What assets don't have to be probated?

Many assets don't need to go through probate. These include:

- Assets in a Living Trust;
- Assets held as joint tenants;
- Assets held by husband and wife as community property with right of survivorship;
- Bank trust accounts;
- Real estate held under a Revocable Transfer on Death Deed;
- Assets with a designated beneficiary, such as life insurance, annuities, IRA's and other retirement plan benefits, and "pay-on-death" accounts; and
- Assets passing to a surviving spouse.

If your assets which would be subject to probate are less than $166,250, the estate does not need to go through the formal probate procedures; we can use a simple form to transfer the ownership.

How much does probate cost?

The cost depends mainly on the size of your estate and the person who serves as Executor. There are fees payable to the probate court (these can run from several hundred dollars to several thousand dollars) and to a court appointed appraiser (who charges 0.1% of the value of the assets appraised). The main costs of probate are the fees which are payable to your Executor and the Executor's lawyer for the work they do.

In California, the law sets a fee for the Executor and the same fee for the Executor's lawyer, for "ordinary services." The fee is based on the estate's gross assets and income. The fee is:

4% on the first $100,000,
3% on the next $100,000,
2% on the next $800,000,
1% on the next $9,000,000,
lower fees above that as determined by the Court.

Thus, a typical fee runs about 1% to 2% of the assets. If you name Co-Executors, they split one fee. (Sometimes a family member or good friend who serves as Executor will waive the fee.) The fee is the same no matter how long the probate takes, although as more income is earned, the amount of the fee will increase. The Executor and the Executor's lawyer may also charge "extraordinary fees" for extraordinary tasks, such as tax work, litigation and sales of real property.

Will I save money by avoiding probate?

Avoiding probate may not save you much in fees. If you name a family member (for example, your spouse or a child) as Executor, that person may decide not to charge a fee.

Many people set up Living Trusts thinking that this will save fees. However, a person who would charge for being an Executor probably would charge for serving as Trustee of a Living Trust. Lawyers generally charge on an hourly rate basis to help administer a Living Trust following a person's death, and there is less legal work to do with a Living Trust compared to a probate. So, using a Living Trust will probably save your heirs money.

Can/should I avoid probate?

It often makes sense to avoid probate, especially by setting up a Living Trust. This is especially true if:

- You are elderly or suffer from a debilitating illness;
- You own real estate outside the state where you live;
- You don't want your Will or your assets to become known to the public;
- You own a sole proprietorship; or

- You want your beneficiaries to begin receiving funds as soon as possible after your death.

Most of the expense that occurs with a probate will arise even if there is no probate, and most of the time delay in a larger estate before the estate is finally closed will occur even if probate is avoided (due to issues with the estate tax).
Many people mistakenly think that avoiding probate means that their families won't have to pay death taxes. <u>This is not true; there are no tax savings from avoiding probate!</u>

The probate procedure provides for court supervision. Although this may be unnecessary in most situations, it is helpful in estates where someone has acted fraudulently.

LIVING TRUSTS

What is a Living Trust?

A "Living Trust" is like a separate entity in some ways (for example, a partnership or corporation). The person who sets it up is the "Settlor" or "Grantor" or "Trustor." The "Trustee" manages the assets you transfer to the Trust (the "principal") for your benefit while you are alive and for those beneficiaries you name after your death. You can be your own Trustee.

Does having a Living Trust avoid probate?

<u>**Just signing a Living Trust will not avoid a probate**</u>. A Living Trust allows you to avoid probate only if you transfer the legal title to most of your assets to yourself as Trustee of your Living Trust during your lifetime. (Remember, assets held in your name directly are generally subject to probate; and assets held in joint tenancy or which are controlled by a beneficiary designation probably will avoid probate.) Thus, if you set up a Living Trust and transfer most of your assets to it during your lifetime, then on your death a probate won't be necessary because you don't own any significant assets as an individual.

Do I still need a Will if I have a Living Trust?

You still will need a Will to deal with assets that have been left out of the Living Trust (for example, because you made a mistake and forgot to transfer them into the Trust). This kind of Will is called a "Pour-Over Will," because it pours all your assets into the Living Trust at the end of the probate process.

Can I control assets in a Living Trust?

You can control all of the assets in your Living Trust. You can be the Trustee. You'll keep the right to cancel the Trust or change the Trust provisions, and you can spend your money and make investments any way you want.

Can my family use assets in my Living Trust immediately

Your successor Trustee can start managing your Trust immediately after your death. The successor Trustee then can use the assets in your Living Trust for your family's benefit.

after my death?

There would be some delay in a probate.

Does a Living Trust save estate taxes?

A Living Trust can offer options to married couples for minimizing estate taxes, but assets in a Living Trust do not avoid being included in your taxable estate.

What if I become incapacitated?

Your successor Trustee can start managing your Trust immediately if you become incapacitated. Your successor Trustee will handle your affairs for your benefit. This avoids the need for a conservatorship (another type of probate court proceeding). However, there are other things you can do to avoid a conservatorship, such as signing a Durable Power of Attorney (for finances). Also, community property isn't subject to a conservatorship if one spouse is still competent.

Will a Living Trust protect my assets from my creditors?

A Living Trust will not protect your assets from creditors. However, a Living Trust (or a Trust established under a Will) can protect the assets held for your beneficiaries from their creditors. There are other planning techniques available that can, in some cases, protect your assets from your creditors while still making those assets potentially available to support you if you have financial problems.

Should I have a Living Trust?

A Living Trust is good for most people, but not everyone. The decision to create a Living Trust depends on many factors such as your age and health, the size of your estate, whether you own assets in more than one state, the type of assets you own, your desire to save some administration fees, your desire to avoid a conservatorship if you become incompetent and your desire to keep information about your assets and bequests private.

How should I hold title to my house?

Usually, you should not hold the house in joint tenancy. The best way to hold title to your house depends on many things:

- Whether you own the house alone or with another person;
- Whom you want to inherit the house when you die;
- Your income tax basis in the house; and
- Whether you have a Living Trust

If you have a Living Trust, usually the title to the house should be in the name of the Trustee of the Living Trust.

How do I put assets in my Living Trust?

You must sign various papers to transfer your assets. You transfer real estate into the Trust by signing a deed. (There will be no Proposition 13 reassessment on a transfer of real estate to the Living Trust.) You transfer to the Living Trust your partnership interests, securities and deeds of trust by signing "assignments." Your existing bank and savings accounts (other than a small operating account) should be closed, and the cash should be transferred into new accounts owned by the Living Trust. You should close your existing stock brokerage accounts, and open new ones in the name of the Trust.

TRUSTEES, EXECUTORS AND GUARDIANS

Who should be my Executor and Trustee?

The Executor and Trustee should be someone you trust and who has "business" sense. This may be a family member or a friend, or you may wish to select a bank or trust company, or an individual professional trustee.

Whom should I name as the guardian of my minor children?

Choosing a guardian for minor children is a very hard decision. The guardian of minor children should be someone who is willing and able to look after your children and to raise them if something were to happen to you.

You should choose someone the children will get along with and who would have the time to look after your children. Obviously, the guardian should be someone who has a similar philosophy to yours on how to raise children, and who would respect your wishes on such matters as religion and schooling.

If you are considering naming someone much older than yourself (for example, your parents), consider whether they will have the stamina and tolerance for noise and the energy that it takes to raise children through the age of 18. If the guardian lives in another city, how will the children react to the move? Will the children be easily accessible to other members of your family? Is there a big gap in the standard of living you enjoy and that which the guardian enjoys?

DISTRIBUTION

Should distribution to my children be outright or in trust?

A Trust protects young or financially inexperienced beneficiaries, and can save taxes. If you leave assets to a child outright and the child is less than 18 years of age, then a court-supervised guardianship may need to be established to manage the assets for the child. This is both expensive and cumbersome. When the child turns 18, he or she will receive the assets; but it may not be advisable for the child to receive your assets at that age.

California law (the California Uniform Transfers to Minors Act) lets you transfer assets to a custodian who will administer the assets. Ordinarily, the beneficiary gets the assets when he or she turns 18. However, the California Uniform Transfers to Minors Act lets you defer the receipt of the assets by the minor until age 21 (if you make a lifetime gift) or age 25 (if you make a gift at death).

Finally, you can transfer the assets in trust for a minor. The Trustee will make distributions to the child or for the child's benefit according to the distribution requirements in the Trust. You can control the date when the Trust ends, and there is generally no limit on the age of distribution. You can also keep the assets in trust for the child's lifetime. Assets held in trust for a child are protected from the child's creditors and from the child's spouse while the assets are held in trust.

Should there be one Trust for all or should each child have a separate Trust?

Each child can have his or her own Trust, or you can set up one "Pot Trust" for all children until the youngest reaches a certain age. **There are pros and cons to each approach.**

Using separate Trusts means that, if one child goes to a very expensive school or has high medical costs, the other children's shares don't subsidize that cost. Older children don't have to wait for the younger children to grow up, before they receive their inheritances.

A "Pot Trust" insures that the funds are available for all the children while they are growing up and getting an education. For example, if you have already paid for your older child's college education, it seems fair to have your overall estate (the "Pot Trust") pay for your younger child's education after you are gone, as you would do if you were alive. Otherwise, if the estate is divided into separate shares for your children, your younger child would have to pay for his or her education from his or her own share, which your older child did not have to do. When all the children have achieved a certain age, the Trust could be divided into equal shares for the children. The Pot Trust may force an older child to wait a long time to receive his or her inheritance when there is a big age gap between the oldest and youngest child. There is also the risk that one child's needs may exhaust the entire Trust.

When should my children receive their inheritance?

Children should inherit assets when they are old enough to manage the assets. The age depends on your philosophy and the maturity of the child. Some people do not like the idea of ruling from the grave and they provide for distribution when the child turns 18. Others feel that a child should inherit money only when the child is more mature.

It is a good idea to provide for distribution in installments. Most people learn how to handle money only by handling (and losing) it; and most people don't have the opportunity to handle money until they are in their mid 20's at the earliest. A fairly common provision is that the child will receive part of the assets at 30, a further installment at age 35, and a final installment at age 40. If a child were to spend all the assets distributed at age 30, the child would still have the other two installments to enjoy later.

However, some people prefer to set the ages later, to force their children to earn their own living and become productive members of society, or to assure that some funds will be left when the children are in their retirement years.

Finally, some people believe that assets should remain in trust for the child's lifetime, as this will afford the maximum protection against creditors, or a divorcing spouse. Sometimes (especially with large estates) there may be substantial tax benefits if you keep part of the inheritance in trust for the child's life.

PLANNING FOR INCAPACITY

Who can make decisions for me if I am incapacitated?

You should sign a Durable Power of Attorney or a Living Trust now. Otherwise, if you become incapacitated, a court probably would have to appoint a conservator to act for you. California law lists the relatives who have priority in being appointed as your conservator, or you may nominate a conservator while you have the capacity to do so. The court supervision, accounting and reporting requirements are similar to those in a probate estate, except that the court also requires additional investigations and reporting in order to protect the incapacitated person from unscrupulous or inept conservators.

What is a Durable Power of Attorney for assets?

By giving another person your "Power of Attorney," you authorize him or her to sign your name and take other actions for you concerning your assets. A "Durable" Power of Attorney remains effective even if you become incapacitated. Typically, a Durable Power of Attorney only becomes effective when you are no longer able to handle your own affairs, although it can become effective any time you choose.

It is a good idea to have a Durable Power of Attorney for assets even if you have a Living Trust. There are some assets (like Social Security benefits) that you can't assign to a Living Trust, and you may forget to transfer some assets to the Trust (in which case they would not be under the control of the Trustee).

What is an Advance Health Care Directive or Durable Power of Attorney for Health Care Decisions?

With an "Advance Health Care Directive" or "Durable Power of Attorney for Health Care Decisions," you authorize another person (your "Agent") to make your medical decisions for you when you are no longer able to make them yourself. Your physician can act on your Agent's orders without incurring liability for doing so. Your Directive can express your wishes about being kept alive on life support systems if you are in an apparently permanent coma or where there is no apparent hope of a recovery. It can also express your wishes regarding organ donations and the disposition of your remains.

What is a Living Will?

Under California law, the "Living Will" is part of the Advance Health Care Directive, which can state your desire not to be kept alive artificially on life support systems.

Whom should I name to act for me when I become incapacitated?

Typically, you will want to name the same person you choose as your Executor and Trustee to be your Attorney-in-Fact (or "Agent") in your Durable Power of Attorney (for financial matters). This is usually a person you trust and who has some "business" sense.

For your Advance Health Care Directive, however, you will want to name someone who will carry out your wishes regarding your medical care, life support and the disposition of your remains. This person need not be the same person you name to take charge of your financial assets.

ESTATE TAXES

How much are estate taxes?

For 2021, the estate tax exemption is $11,700,000 and the tax rate above that is 40%. The exemption is set to change with changes in the cost of living. In general, estate taxes are taxes imposed on the value of assets which you own when you die. Generally, if the net value of your assets passing to someone other than your spouse or charity is more than the exemption (the "applicable exclusion amount"), there will be a tax payable.

This is a tax completely distinct from income taxes and other taxes. Note that if you own assets in a state other than California, or if you own assets outside the United States, then there can be additional state or foreign estate taxes. California does not impose a state estate tax.

Will there be estate taxes on assets passing to my spouse at my death?

There are no estate taxes on assets passing to a spouse, either outright or in certain kinds of trusts, because there is an unlimited marital deduction for assets passing to a surviving spouse. (However, there are special, complex rules if your spouse is not a United States citizen, despite your spouse's residence or immigration status. Therefore, although all of your assets are included in your taxable estate, any assets passing to your spouse will be deducted in computing your taxable estate, and therefore are, in essence, not taxed. The marital deduction allows for a deferral of estate tax on assets passing to a surviving spouse; all such assets remaining in the surviving spouse's estate at the surviving spouse's death will be included in the surviving spouse's estate, and may be taxed then.

Can my estate get a marital deduction if I control who

You can get a marital deduction for assets passing into trust for your spouse. As long as your surviving spouse receives at least all the income for life from your assets, and no one other

receives my assets after my spouse's death?

than your spouse receives the benefit of these assets while your spouse is living, you can take advantage of the marital deduction and still control who receives those assets at your spouse's death. This entails using a "QTIP Trust" as part of your Will or Living Trust. (If you wish, your spouse can also have the right to receive principal from the QTIP Trust for most living expenses.)

How can I reduce estate taxes on my estate?

There are many techniques for reducing estate taxes. First, you can make "annual exclusion" gifts of up to $15,000 per person each year without incurring gift tax. Married couples can give up to $30,000 to each donee without incurring gift tax. These $15,000 gifts remove assets from your estate for estate tax planning purposes without any gift tax consequences. (You don't get an income tax deduction for making the gift, and the recipient doesn't have to report the gift as income.) You can make additional "tax-free" gifts by <u>directly</u> paying for school tuition, medical bills, or both, of your family and friends. These gifts must be made directly to the educational institution or medical service provider, and not as reimbursement to your family member or friend.

Second, by giving away assets over the $15,000 annual exclusion gifts, you remove appreciation and income on gifted assets from your estate, and that appreciation and income will not be subject to estate tax when you die. Gifts over the annual exclusion, up to $11,700,000 over a lifetime, won't give rise to a tax, but will reduce the amount you can give away tax free on your death.

Third, for married couples with net assets worth more than the lifetime exclusion amount, the estate plan can provide for the creation of separate "subtrusts" on the death of the first spouse, to preserve that spouse's exclusion. Also, a deceased spouse's unused exemption is "portable" and can be preserved by the surviving spouse in most circumstances, to be used at the second death. But, in many cases, the creation of a tax-saving "Bypass Trust" on the first spouse's death can eventually save more in taxes and, in estates under $11,700,000, can eliminate the need to file an estate tax return on the first spouse's death. (An estate tax return must be filed to make the first spouse's exemption "portable.")

Finally, there are many more sophisticated plans that you can use to reduce these taxes for larger estates. A memo that discusses some of these techniques is available on our web site, www.hswlaw.com.

GIFT TAXES

Should I make gifts?

You should make gifts if you want to and you can afford to. If you have more than enough assets to enjoy for the rest of your life, including emergencies, you should consider making gifts. Making lifetime gifts is an easy way to reduce estate taxes. Lifetime gifts will retain your income tax basis (whereas gifts made at your death receive a new basis equal to the value of the asset as of the date of your death).

How much can I give without any gift taxes?

Each person can give $15,000 to each beneficiary each year without any gift or estate taxes. In addition, you can pay school tuition (directly) for a person, and can pay another person's medical bills (directly), regardless of the amount. Finally, up to $11,700,000 given away during your lifetime will not give rise to any gift taxes (although a Gift Tax Return must be filed to report the gift). Any gifts in excess of the $15,000 annual exclusion (other than direct payment of educational and medical costs) "chip away" at your lifetime estate/gift tax exemption of $11,700,000, so that less of that exemption will be available at death. Lifetime gifts in excess of that $11,700,000 exemption are taxable at 40%.

Are gifts to my spouse subject to gift taxes?

You can make gifts to your spouse without paying gift tax. Gifts to spouses are technically subject to tax. However, there is an offsetting unlimited marital deduction for gifts made to a spouse. (Again, there are different rules if your spouse is not a United States citizen.)

Can I make gifts in trust for my spouse and children rather than outright?

You can make gifts to a spouse or child in trust. Generally, the $15,000 annual gift tax exclusion doesn't apply to gifts made to a Trust. However, you can use that annual exclusion for gifts to an irrevocable Trust if the Trust includes provisions giving the beneficiary the right to withdraw those funds from the Trust, exercisable for a minimum window of time (generally 30 days). If you make a gift to a spouse in trust, the Trust must satisfy certain requirements to qualify for the marital deduction referred to above.

Which assets should I use to make these gifts?

You don't have to make gifts in cash! It is often advisable to give away small interests in real estate or a closely-held business, because the value of those assets can be "discounted" for gift reporting purposes, thus leveraging your gifts.

GENERATION-SKIPPING TRANSFER TAXES

How much are generation-skipping transfer taxes?

For 2021, the generation-skipping transfer tax ("GST") is imposed on transfers over $11,700,000 at a 40% rate.

What distributions are subject to generation-skipping transfer tax?

If the GST is in effect, all gifts and distributions from Trusts to grandchildren, great-nephews and great-nieces, and to unrelated persons more than 37-1/2 years younger than you, are subject to the generation- skipping transfer tax. As with gift and estate tax, there are some exemptions and exclusions. Very simply, $15,000 annual exclusion gifts (other than those to certain trusts) are exempt, and there is an exemption (in 2021 it is $11,700,000) available for each individual to pass on to his or her heirs. If a child predeceases you, his or her children "move up" a generation for these purposes, so you can leave the assets to those grandchildren without incurring this tax.

Should I make gifts during my lifetime or at my death to my grandchildren?

Gifts made during your lifetime using your $15,000 annual exclusion may save both estate and generation-skipping transfer taxes. If the GST is in effect, this combined saving might be as high as 64¢ on the dollar. It is therefore desirable to make these gifts if you are in the financial position to do so. Similarly, you should consider optimizing your $11,700,000 exemption by giving some or all of this amount to grandchildren. Alternatively, you could allocate this amount in trust for children during their lifetimes and then to grandchildren after the children die.

LIFE INSURANCE

Do I need life insurance?

Life insurance is an important part of many estate plans. It provides cash liquidity at the time of death to pay estate taxes. It can provide an "instant estate" to replace your salary, and thus protect your family. Finally, because it is possible to have the proceeds of life insurance excluded from your estate for estate tax purposes, it is an effective way of getting a large chunk of assets out of the estate tax.

How much life insurance do I need?

The amount of life insurance will depend upon the following factors:

- The amount of cash that your heirs will need to pay taxes and expenses;
- The standard of living that you want your heirs to have; and
- The available cash that you have to pay the premiums.

What does life insurance cost? What kind of life insurance should I buy?

The cost of life insurance will vary according to the type of insurance, your age and health, and the amount of protection. Generally, the type of life insurance you buy will depend on how long you plan to keep the coverage. For example, if you're buying the insurance to help cover death taxes on a valuable closely-held business, you would normally take out a policy which builds cash values (such as a whole life or universal life policy) because the need for cash likely is not going to go away. If you are taking out a policy to supply a standard of living for your children until they finish college, then a term insurance policy (which does not build cash values) may be sufficient because you can anticipate that these heirs will become self-supporting after a certain time.

Because estate taxes are usually payable only after the death of a surviving spouse, if you are buying insurance to help pay the estate taxes, you may want to consider buying a "second to die policy." This kind of policy pays off only after both spouses have died, but it is usually cheaper than buying a policy on the life of one of the spouses. Term insurance (which doesn't build cash values, and gets extremely expensive once you get into your 70's) can be bought on an annually increasing premium basis. Alternatively, you can pay somewhat more and have the premium fixed for 10 or 15 years.

Is life insurance tax-free?

Usually, life insurance is income tax free, but may be subject to estate tax. Life insurance proceeds will be subject to estate tax unless you have no "incidents of ownership" over the policy, and the policy is not payable to your estate. Thus, you should not own or control the policy and it should not be payable to your estate.

Who should be the owner of my life insurance?

Life insurance can be free of estate tax if the policy is owned by the person you want to name as beneficiary, or by an "Irrevocable Life Insurance Trust," often called an "ILIT." An Irrevocable Life Insurance Trust generally cannot be changed after it is created, except by agreement of all beneficiaries and the creator of the trust, or by court order. Thus, it is very different from a Living Trust. However, not everyone wants to give up ownership and control of their insurance, especially where the policy has a large cash value (against which you could borrow money if you own the policy directly), or where the insured's children are very young. If you own the policy directly (not in an ILIT), the proceeds of the policy (the death benefit) will be subject to estate tax when you die (but, of course, subject to the possible use of the marital deduction and the "applicable exclusion amount" discussed above). In most cases where you or your Living Trust owns the policy, it does not make any difference whether the beneficiary is your surviving spouse, a Trust under your Will, or your Living Trust. It may be advantageous to make your Living Trust the beneficiary of the policy if you want to fully fund a Bypass Trust at your death (as discussed above). In any case, your Living Trust generally should be the "contingent beneficiary" if the first beneficiary dies before you. Generally, you shouldn't name your estate as the beneficiary, since the proceeds would have to go through probate.

RETIREMENT PLANS

What taxes are there on IRA's and other retirement benefits?

There are income taxes and estate taxes, and there can be excise taxes, on IRA and retirement plan benefits. When you or your beneficiary withdraws money from the plan, there will be income tax payable on the withdrawn amount. The IRA and retirement benefits will also be subject to estate taxes. **The combined tax effect may be over 72¢ on the dollar.** Excise taxes can apply if you take money out of the plan before age 59-1/2 (with some exception) or if you don't take out certain minimum amounts each year generally beginning at age 72.

Who should be the beneficiary of IRA's and other retirement benefits?

The choice of beneficiary can affect how much you must take out of your plan during your lifetime, and who will inherit the plan assets when you die. The choice of beneficiary is a complicated decision that can't be answered easily. If you are married, your spouse may benefit from these plans without paying any estate tax, and may be able to defer paying income taxes by delaying the time when the spouse must start receiving the benefits.