A Layman's Guide to Navigating Estate Planning

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Disclaimer

This book is intended to be a resource for you as you navigate the various aspects of an estate plan. It is written in plain language, as much as I can. I have included real world stories of clients of mine, that helps you to understand the complexity of the issues along with a basic understanding of the law. This book does not create an attorney-client relationship, and you should not think that I am your attorney, unless an engagement is signed and payment for services is provided.

Please Note that there will be many acronyms utilized throughout this book. I use them not to confuse you, rather to have you become accustomed to them as professionals you speak with will use them. I will always define the acronym the first time it is used.

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Why I Wrote This Book

If I had a quarter, yes I know inflation from a nickel, every time I heard someone say that they have a Will and that is all the need I would be a very wealthy person. There is such a common misconception that a Will avoids the dreaded Probate. The truth could not be further from the myth. Only a trust would avoid the Porbate Court.

For this reason I wrote this book that helps to dispel some myths and helps to explain the process.

Please do NOT use this book as anything other than informational purposes only. It should NOT be used as a legal how to guide. You have not engaged me as an attorney to represent you, by simply obtaining this book. My office requires a signed engagement letter and payment for proper representation.

If you have any questions, please feel free to pick up the phone and call our office, or send us an email. We are happy to talk with potential clients. That is why we are in business.

Estate Planning

In order to understand estate planning, it might be helpful first to understand its function. Estate

planning is nothing more than having some advanced planning if an individual should become incapacitated, and a Revocable Trust to have the assets pass to the family outside of Probate.

Advanced Directives

Advanced Directives are really a collection of three critical documents. If an individual does not have these documents, then a Guardianship would be necessary. (Guardianship is the other evil step child, after Probate, that is best avoided. The mental anguish and cost is tremendous for Guardianship, especially when you consider the cost of created a well planned Estate Plan that avoids both at a fraction of the cost!) The Power of Attorney enables a named person to act on behalf of the individual in respect to financial institutions, and government agencies. A well written Power of Attorney also enables the person to do some advanced Medicaid planning, as well as having the ability to choose residencies for the individual.

The Healthcare Directive allows the named person to make health care decisions for the individual.

Finally, the Living Will, which is different than a regular Will and should not be confused, is a statement from the individual as to his or her desire regarding life support.

These three documents together create the Advanced Directives. If you do nothing else, please get these documents completed. They are not costly, and can save you thousands of dollars in

Guardianship. They are also so critical especially for a senior to have them completed and accessible.

Revocable Trust

The Revocable Trust is the centerpiece of the Estate Plan. It does the same thing as a Will in declaring an individual's desires regarding their assets. However, it also goes a step further in avoiding Probate and enabling staged distributions to beneficiaries.

Distribution

The Revocable Trust is very flexible. It can be created to have staged distributions to the beneficiaries, or kept in trust in perpetuity. A staged distribution is whereby the trust is distributed at regular intervals, usually 25 years old, 30 years old, and the last distribution at 35 years old, to the beneficiaries. A well drafted Revocable Trust would also have the ability for the Trustee to distribute to a beneficiary for a life event such as tuition for college, marriage, purchase of a home, or start a business.

The other option for distribution is to have the assets remain in the trust indefinitely and distributed as needed to the beneficiaries. This would protect the beneficiary from any creditors who could simply wait for a mandatory distribution at a staged distribution. This method also enables the Trustee to slow down or speed up the distributions based on the maturity level of the beneficiary and the need of the beneficiary.

The most important person of a Revocable Trust is the Trustee. The initial Trustees are almost always the husband and wife. It is then a question of which family members would follow should

both parents pass away. The choice should not be taken lightly. I often have clients who choose a Trustee based on a decision not to offend someone. I think that this is the wrong approach to choosing a Trustee. Another important consideration should be made if there are minor children. I never recommend the same person who becomes the named guardian of a minor child also be the Trustee and control the trust assets. I know this sounds a little crazy, but I have seen families insist on having the same person, only to have the minor child come to me years later as an adult and the trust assets have been depleted in upgrading the guardian's personal home.

Equal is Not Always Fair

When it comes to distributions, equal is not always fair. When I say this to clients, the look I almost always get is nearly comical. Huh? Well, lets use an example from a client. Husband and Wife have three children ages 20, 18, and 17. They have life insurance, of course, and created a trust with equal distributions to each of the kids in a staged distribution manner at 25, 30, and 35. As good parents, they pay for college for their children, and graduate school. When the kids are 22, 20, and 19 the parents go on a vacation to Fiji for a week. Unfortunately, there was a tsunami and the parents perished in the tidal wave. So, the life insurance is paid out, to the trust with the new trustee, the brother of the husband, dutifully takes on the responsibility of being a trustee. He pays for the remaining two years of college for the middle child, and the remaining three years of the youngest. The money comes from each child's respective shares of the trust. This might seem fair at first glance. However, lets think about this for a second. The eldest child had his college tuition and living expenses paid from the INCOME of the husband and wife. NOT from the life insurance; while the youngest two kids are dipping into their inheritance to pay for college. So, lets use some numbers to get a clearer picture. The life insurance was for $1 MM, meaning $333

K for each kid, and college tuition and expenses is $50 K per year. So, the oldest child will get the full $333 K from the life insurance, the middle will get $233 K, and the youngest only $183K. This obviously is not really fair, but it is equal. We counsel our clients in these issues and help them arrive at their own decisions.

Special Needs Trusts

The law, meaning the statutes as they are presently written, are not perfect. If they were, then we would not have any trials. For any particular issue, we would look in the statutes, determine which ones apply and allocate fault. Special Needs Trusts fall into this weird never world where it is not always clear cut. So, imagine an adult child, whose parents just passed away. Further imagine that this adult child had a horrible car accident a few years prior to his parents passing, and he was left a quadra pelagic and on Medicaid. So, upon his parents passing, he inherits the estate, including a $500 K life insurance policy. Well, if takes the money, he will lose his Medicaid. He could of course create a Special Needs Trust, but since the money is now his, it MUST be a First Person Special Needs Trust, which means that when the adult child passes away, any money remaining in the Special Needs Trust will go back to Florida Medicaid as reimbursement. Imagine further that the adult child was married himself, with two kids. They will NOT receive ANY of the inheritance. This horrible scenario is easily avoided with a properly drafted Estate Plan that includes a properly drafted Will and Trust.

Just another reason NOT to go to Legal Zoom and think that you could do it yourself with some forms. You are not paying for the documents when you have an Estate Planning attorney draft your Estate Plan; you are paying for the knowledge and expertise provided.

Homestead

There is a split of decisions among Elder Law attorneys regarding the Homestead as it relates to the Estate Plan. While an Estate Plan would avoid Probate, some Estate Planning Attorneys recommend that the family file a Probate, even if there are not any assets. The reason is that a creditor has a limited amount of time in order to make a claim against an estate for monies owed. If a Probate is not filed, then the time frame is two years for a creditor to file a claim. Meaning, a creditor could conceivably come back to the family after one year demanding payment for monies owed. If a Probate is filed, then the time frame is greatly reduced to three months. This is helpful for the family in their ability to safely disburse any monies to the beneficiaries without any worries of future creditors potentially knocking on the door. This type of probate is much easier to handle from a legal perspective because the family is not waiting on the judge to sign orders for them to get any inheritance.

I normally place the homestead into the Revocable Trust. The reason is that any homestead exemptions are not lost, while the trust would provide a better avenue for the trustee to disburse any proceeds if the house should be sold.

Capital Gains

So Capital Gains is NOT an Estate Tax, nor an Income Tax. It is a tax placed on property, real property like a home, stocks, or a business for example, that is taxed when the property (again, home, stocks, business, etc) is sold. The tax amount is 15% for a long term or 20% for short term on the capital gain. Let me say that I can not predict the future, specifically what President Biden might do with Capital Gains, so this is written on the current standards. The differentiation of

short term and long term is how long the property was held. The threshold is one year. So, if you imagine a stock that was purchased on August 1, and sold the following February 2, that would be a short term Capital Gain at 20%. However, if the stock is held through the following August 2 and then sold then the Capital Gains is 15%.

So lets look at an example to understand this concept. Imagine that you purchased a rental home in 2010 for $150,000. Fast forward ten years and the house is sold for $200,000. The Capital Gains is $50,000 ($200,000 - $150,000) which would mean a long term Capital Gain Tax of 15% since the property was held for more than one year. So, 15% times $50,000 equals $7,500 of Capital Gains Tax.

Now, you are asking me why am I telling you this information. Well, I have clients who attempt to do their own estate planning and do a quit claim deed for a home, thinking that they can save on Probate Costs. Well, there is an IRS code that states that if a property (again home, stock, business, etc) is inherited, then there is no capital gains!! So, if you do a properly drafted Estate Plan, then the whole issue of Capital Gains would be nullified.

Probate

Probate is a court process that has an individual's assets from them to their family. Any asset that has a title to it, such as a home, or car, or any asset that has designated a beneficiary, like a bank account, must pass through Probate, unless some pre-planning was performed. There is a common misconception that a Will does not need to go through Probate. Unfortunately, that is incorrect. A Will still needs to pass through Probate. Only a trust would avoid probate.

The purpose of this book is not to explain Probate in any great detail, so I am only providing an overview of Probate.

Probate Estate

Really, all assets that are not already directly transferred to family members either through a Trust, a Deed on a home, or direct beneficiaries to bank accounts and such, becomes the Probate Estate.

Probate should be avoided for two primary reasons. The first is the cost. Florida Legislature has mandated what the Probate fees are for the family. They are 3% for an estate less than $1 million, and 2.5% for estate greater than $1 million. As you can imagine this becomes very expensive. An estate worth $750,000, which is not improbable given the value of a home, some life insurance, maybe some IRA, etc., which would cost $22,500 in Probate costs. For this reason, most clients would want to avoid this situation.

The second reason is time. Probate is an incredibly long process. It is not uncommon for Probate to take two years to complete, even an uncontested where family members are not fighting over an inheritance. Finally there are some attorneys who refuse to file a Probate in Miami Dade because of the time delays uniquely inherit with Miami Dade.

Avoid Probate

Depending on the asset, there are two very easy ways to avoid Probate. The first method is designed for titled assets, such as real estate, and cars. The second is for financial instruments like bank accounts, retirement accounts, and Life Insurance.

The use of a Revocable Trust helps the family from avoiding Probate. The Revocable Trust designates the wishes of the individual, meaning who gets what and when, while avoiding Probate. It really is a great tool that is not overly complicated or expensive to implement.

The second method is also an easy and inexpensive method of avoiding Probate. The individual just designates a beneficiary of the account should the individual pass away. There is a drawback to utilizing this method in that the beneficiary is given the money outright, which could be a potential problem from the beneficiary's creditors such as divorce, or bankruptcy.

Probate Process

The Probate process is relatively straight forward. A Petition is filed with the court with the Personal Representative, who is usually a close family member. The Personal Representative has

a fiduciary duty to the other beneficiaries not to "waste" the estate assets during Probate, and fairly divide and distribute the assets according to the Will.

Admitting Will

The first step is to have the existing Will admitted into the Probate Court. This is generally a simple process, if the original Will is available. If not, then the two witnesses who signed the Will must testify to have the Will admitted. For this reason, a good estate planning attorney will maintain the original Will in the office.

If there is not a Will, or a copy could not be admitted, then the line of succession for inheritances are a spouse, children, siblings, parents, grand parents, aunts and uncles. Generally, a surviving spouse would receive half, and the children would then inherit the other half, in equal shares.

There is also a statute called the Elective Share, which means that if an individual decides to remove a spouse from any inheritance, then the surviving spouse could still elect to have an elective share, which is 1/3 of the gross estate in Florida. So, if a person really wants to disinherit a spouse, the best method is a divorce.

Depository Accounting and Final Disbursement

The next steps, aside from having the Personal Representative approved by all parties, is to have the Personal Representative deposit any monies into a bank account established specifically for Probate. We call this a Restricted Depository, because only with a Court Order can any money then be distributed. The Personal Representative also files an accounting with the court listing all

of the assets of the individual. Finally, a Final Disbursement is filed to divide the money and disburse to the beneficiaries.

While this does not sound complicated, it does unfortunately take an incredibly long time to have a Probate finally closed. This is primarily because of the lack of judges in Probate, and the inefficiency of the court employees. In Broward, there are four Probate Judges for a County of two million people. Counter that to the 16 family court judges for divorces, and you can see why it takes so long.

Asset Protection

What is Asset Protection? It is simply protecting your assets (or "stuff" such as your home, and investments) from creditors. Creditors in general is someone to whom you owe money. It could be a bad business deal, or a car accident. Your next statement is going to be, but I have car insurance. Correct!! As I describe Asset Protection to clients, imagine a medieval castle. There is the moat, the draw bridge, the castle walls, and finally the knights inside the castle. These are all layers of protection. Does that mean that a well fortified castle is 100% impregnable? Of course not. If so, we never would have had wars as the attacking side would have realized that the effort would be futile. Instead, they are merely a deterrence against an attack. Asset Protection should operate just like a castle, and the first line of defense is always a good insurance policy.

The next line of defense is tailored to your needs. If you have rental properties, and they are all in your personal name, then you are not protected. Even worse is that if there is an accident at one rental property, then all of the properties are at risk of suit. We create a Limited Liability Company to shield the rental properties from the creditors. The Capital Gains of a property held in a Limited Liability Company could be avoided, if it is properly drafted. Another reason not to go through a self help like Legal Zoom.

Another example of Asset Protection is an Irrevocable Trust. This is even more impenetrable than a Limited Liability Company, but as you could imagine, it adds more complexity to the equation. We use Irrevocable Trusts typically for some of the assets, if the individual is in a high risk profession subject to suits. For instance, a doctor might want to place his fishing boat into an Irrevocable Trust.

Business Succession

So the fist step in a business succession plan is often overlooked. The business needs to be valued in order to design the succession plan, especially if it is a partnership. Imagine a repair shop, or a dental office, where there are two partners working in the business. If one of the partners passes away, then how does the surviving partner continue? Does he or she now have a new partner of the deceased partner's spouse? How much of a payout is necessary?

These are all good questions. There is not one answer, unfortunately. A business valuation could be done with market comparables, not unlike a home appraisal, but that is not always accurate. How does it properly incorporate an Account Receivable heavy business, such as a medical practice, into the valuation? What percentage of AR gets counted?

Another method is simply value the inventory, equipment, accounts receivables, and the bank accounts, and add those up for a value. For obvious reasons this is not a true value of the business.

A business appraiser could also arrive a business value. However, it might be biased and three would likely be needed, and an average of the three would be used. This could become expensive.

Another method is an income approach. The income approach utilizes the net income, and multiplies it by some number, to reach a valuation. Personally, I use the income approach with some modifications. I use a rolling 3 year average of Net Income, then I add back officer distribution, taxes, depreciation, and interest. That provides an average Net Income. Then I utilize the Risk Management multiplier for the industry, and business size. That provides a multiplier,

which does not really change over time. Now that we have an initial value, and future multiplier, we can now address how to pay for the business succession.

So, if there is a death of a partner, then the business could have Life Insurance to pay the deceased partner's family the value of their portion of the business. Utilizing the multiplier number, the owners should update their life insurance policies annually, to make sure that there is a enough life insurance. Recall, that a business is dynamic, and hopefully growing every year.

None of this could be accomplished with a LLC document from Legal Zoom. Another good reason to utilize an Estate Planning attorney.

Tax

This is always an issue, naturally. What are the tax implications of passing a business to a family member or a partner? Well, as with any asset, there is capital gains tax if it is sold. If the owner wants to sell the business to a family member, then we normally recommend a self canceling note with an Irrevocable Trust, to effectively eliminate any capital gains.

If the business buy out occurs with a life insurance, then there is a potential capital gains, which again the Life Insurance would cover those expenses.