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The 50+ Divorce

A Handbook for Clients

How the outcome may affect your:

- etirement
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What Will Be—Now & Forever

Divorce means a new lease on life and a fresh look at your estate plan

BY LYNNE S. HILOWITZ

[T]he time to address estate planning is during or shortly after your divorce. Sound estate planning makes for a smooth and tax-conscious transition of assets to your heirs upon your death. A new or updated will or estate plan will help establish (1) the maximum amount your soon-to-be ex-spouse will get should you die before the divorce is final (assuming that you have not signed a prenuptial or postnuptial agreement); and (2) prevent your soon to be ex from inheriting your estate because you failed to change your beneficiary designations and the titles to your property.

Take steps now to address the following:

Joint ownership and/or beneficiary designations. Talk with your lawyer about removing your ex-spouse (or soon-to-be ex) as a beneficiary on *everything* you own. For example, life insurance, all financial accounts (including, but not limited to, bank accounts, individual retirement accounts (IRAs), pensions, stocks, mutual funds, bonds, etc.); safe deposit boxes; revocable and irrevocable trusts (consider dissolving or not funding irrevocable trusts for which you cannot change the beneficiary). Note: You may want to consider making your children the beneficiaries of your IRA, rather than your estate, to avoid income taxes due upon your death. Beneficiary designations should be in the nature of a trust to deal more effectively with contingencies.

Change fiduciary designations, such as executor/personal representative, lifetime or testamentary trustee, guardian for minor children, agent-in-fact for your power of attorney, and your health-care proxy or agent (if you do not want your ex-spouse to make decisions for you, such as whether to "pull the plug" or determine whether you are incapacitated).

Trusts for children become even more important upon divorce. Consider the amount of wealth you will transfer at your death and evaluate (1) the necessity of a trust and (2) the duration of the trust. Many clients opt to leave a child one-third of the principal of a trust at age 22, one-half of the balance at age 25, and the remainder at age 28 or 30. Caution your children to keep any inheritance separate from monies to be shared with a spouse or future spouse. If the child should later divorce, any inheritance that has been "commingled" with marital monies will be subject to division with a spouse. It also is imperative to keep earnings separate from an inheritance. Having just been through a divorce yourself, you can readily understand the seriousness of this issue.

General rules

A "will" (formally called a "Last Will and Testament") is a written document in which an individual (the "testator," if male, "testatrix," if female) instructs how property should be distributed upon his or her death, appoints individuals (fiduciaries) who will administer the terms of the will, and sets forth instructions. A will *does not dispose of all* property. For example, property owned jointly with another person passes automatically to the surviving owner. Another example of property passing "outside of will" or by "operation of law" is insurance that is payable to a named beneficiary (*i.e.*, other than to the decedent's estate). Yet another example is property held in trust for a child. Upon the death of the decedent, the property or money belongs to the child.

The terms used to differentiate between property of a decedent passing through the will, or outside the will, are "probative assets" and "nonprobative assets," the former being property subject to a will, and the latter being property not subject to the will. Beneficiary designations are not as powerful as will clauses because a will can be more explicit and detailed about contingencies. You also can designate more comprehensively the payout ages and distribution methods for assets passing to children and/or grandchildren.

A Marital Deduction: A married person can pass an *unlimited* amount of property to a spouse during one's lifetime or at death without triggering taxation. This is due to the "marital deduction." According to federal estate tax rules, all monies left by one spouse for the benefit of another are deductible from the adjusted gross estate of the deceased. For example, if a spouse's gross estate were valued at $1.6 million, after deducting administrative costs and funeral expenses of $100,000, the adjusted gross estate would equal $1.5 million. If the deceased left $500,000 or more to a surviving spouse, the taxable estate would be reduced to $1 million. With a "unified credit trust," the federal estate tax would be zero. Obviously, the "marital deduction" is one of the most important devices for estate and tax planning. If there is no spouse, there can be no marital deduction and no postponement of estate taxes. The only saving grace as far as estate taxes are concerned will be application of the unified credit.

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A Unified Credit or Federal Exemption: A "unified credit" offsets gift and estate taxes. An estate tax is imposed on a person's estate based on the value of the estate assets. The value of assets that will escape federal estate taxes in 2008, for example, is $2 million. The applicable unified credit amount will be applied against $2 million of assets to produce a zero federal estate tax. (This does *not* include state estate taxes.)

Lifetime gifts in excess of the "*annual* exclusion amounts" generate a gift tax in addition to the estate tax. The amount of the annual exclusion from gift tax is currently $12,000 or $24,000 for combined spousal gifting. For gifts made after the year 2001, the applicable total lifetime gift-tax exclusion amount is $1 million. No increases in the gift-tax exclusion are scheduled. If gifts are made after the year 2009, the top gift-tax rate will be the same as the highest individual income tax rate.

Residuary Bequests: These cover all estate assets not disposed of elsewhere, either by specific or general bequests. Usually such a provision addresses all property not otherwise disposed of, conditional gifts that fail to take effect, and legacies that are renounced. The residuary bequest may be made in some wills or in a trust, and sometimes are in the form of an extended trust arrangement providing for children and grandchildren.

Fiduciary provisions

A "fiduciary" is a general term for a person named as an executor, trustee, or guardian under a will. Fiduciaries may be individuals or banks, one person, or several persons acting in the same capacity. Every person must name an *executor*, and if the will contains any trust provisions, a *trustee*. *Guardians* are normally appointed only when minor children are involved. In addition to naming the initial fiduciaries, substitute fiduciaries must be named in the event the original fiduciary has died or is incompetent or unwilling to serve.

Executor (or Executrix): The "executor" is the fiduciary named in a will that has the responsibility to cause the will to be probated, to collect the assets of the estate, and to dispose of them according to the will. The executor has the responsibility

of filing federal and state estate tax returns and income tax returns, filing a final accounting, disposing of claims against the estate, and many other details, as set forth in the will, sometimes even including funeral arrangements for the deceased. Where the testator is the owner or partner in a business or businesses, the executor may have the additional responsibility of running the business or disposing of it. The duties of an executor may extend from several months to several years, depending on the assets of the estate and the latitude given by the deceased.

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Trustee: A "trustee" is a fiduciary that is given legal title to property disposed of by trust. The trustee has the obligation to obtain the trust property from the executor of the will and, thereafter, invest it according to the powers granted in the will. The trustee must periodically account for trust assets and must pay or apply the interest or profits earned by the trust principal as specified and to the person specified in the trust. Often a trustee has discretionary powers. For example, if the deceased makes a gift in trust for a minor child and directs the trustee to pay only the income earned by the trust principal to the child until he or she reaches majority (the age of majority varies by state), with the additional authorization that if the trustee believes it is in the best interests of the minor, he may pay part of the money before the child reaches the age of majority. This authority is common where the deceased parent was particularly concerned with the education of an infant.

Guardian: A "guardian" is a fiduciary appointed to take custody of minor children and the children's property. A surviving spouse generally is the guardian of infant children by law. Where both spouses die, the will or trust must appoint guardians and alternate guardians. Exercise extreme care in appointing guardians because, in effect, a guardian will replace the parents, and the children will live with and become members of the guardian's household. In selecting a guardian, consider his or her age, views on education, physical capabilities to cope with the children, and whether he or she will accept the full responsibility of the position.

In the case of a divorce, a surviving parent usually will be the guardian for the couple's children. However, a will or trust can designate a guardian *of your children's property*, which they are inheriting from you. This guardian is known as the "guardian of the property." This guardian does not have to be your ex-spouse and often is not.

Health care/estate planning tools

A Living Will: This is a document that confirms end-of-life wishes, such as whether you want to be kept alive by artificial means if there is no likelihood of recovery to a meaningful life. It may contain organ-donation wishes and directions regarding hospital stays or home care in the final days of your life. Some states have living will statutes.

A Health-Care Proxy: This is a document that appoints an individual(s) as your agent(s) to carry out your health-care wishes contained in a living will. Some practitioners combine a living will and a health care proxy in the same instrument.

A Durable Power of Attorney: This is a document that delegates to another responsibility to make gifts, real estate and/or personal property transfers, access your accounts, etc. It should be made "durable" if you wish it to remain effective in the event of your disability. Powers of attorney can be "springing," which means that they take effect at a later date or are effective immediately. A power of attorney is a powerful tool that ends at your death but can be revoked at any time. This instrument can avoid expensive and time-wasting conservatorship/guardianship proceedings.

Conclusion

Seek the counsel of a skilled trusts and estates attorney to help you with your estate plan, and recognize that assets in "joint" names or with beneficiary designations will pass "outside of your will" or by "operation of law." Your newly drafted last will and testament or trust thus will be given *no* effect.

Another important thing to remember is to actually transfer assets to your trust if it is your intention for the trust to own those assets. In other words, if you own real estate in another state, a trust that owns the real estate will avoid "ancillary administration" in that other state. However, a deed from you, as grantor, to the trustee of the trust, as grantee, must be recorded in the state where the real property is located.

Show a thorough inventory of your assets to your estate-planning attorney to avoid any misunderstandings or pitfalls. Provide your attorney with *actual* copies of your deeds, account statements, life insurance beneficiary designations, etc., so that he or she can help you plan your estate. Without this complete inventory, your estate plan may exist in a vacuum. There really is no such thing as a "simple will" because life and the law are both complex. Thus, be guided accordingly in planning your estate. **FA**

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