THE ESTATE PLANNER

March/April 2024

REVOCABLE TRUSTS
Don't forget to fund the trust throughout your lifetime

Will contests don't happen only on TV
Take the proper steps to avoid family chaos after your death

To avoid unexpected tax bills, adequately disclose your gifts

Estate Planning Red Flag
You and your siblings have inherited your parents' home

SHUMAKER

Revocable trusts

Don't forget to fund the trust throughout your lifetime

Many estate plans are built around revocable trusts (sometimes called "living trusts"). These trusts allow you to 1) avoid the time, expense and privacy concerns associated with the probate process, 2) specify how your assets will be managed and distributed after your death, and 3) provide for the management of your financial affairs should you become incapacitated. And because these trusts are revocable, you're free to modify or terminate them as you see fit.

After you've created a revocable trust, you can't simply put it on a shelf and forget about it. It's ineffective unless you fund it — that is, transfer assets to the trust. And funding your trust isn't a one-time task. As you acquire new assets in the future, you'll need to consider whether they belong in your revocable trust and, if so, transfer them accordingly.

Not all assets belong in your revocable trust, however. Indeed, it's important to keep certain assets *out* of your trust to avoid adverse consequences. Let's look at some general guidelines.

Assets to fund a revocable trust

Here are assets that are commonly held in a revocable trust:

A home and other real estate. Most people transfer title to their homes and other real estate to their revocable trusts. To make the transfer, you'll need to execute and record a new deed. If property is subject to a mortgage or other home loan, contact the lender to see if it requires any additional paperwork.

Keep in mind that in most states, revocable trusts provide little or no protection against creditors during your lifetime. So, if asset protection is a concern, you may want to consider other forms of ownership. Another option is a domestic or offshore asset protection trust.

Bank accounts. Bank accounts with substantial balances should generally be transferred to your revocable trust. These include checking and savings accounts, certificates of deposit (CDs), money market accounts and safe deposit boxes. Ask your bank about its procedures for retitling assets in the name of your trust, which typically requires a certificate of trust. Note that in some cases, transferring CD accounts to a trust can trigger early withdrawal penalties. If that's the case, you may want to wait until your CDs mature before making the transfer.

Investments. You can transfer stocks, bonds, mutual funds and other investments to your revocable trust. You'll need to execute transfer documents and, depending on the investment, have certificates reissued. Your broker can guide you through the process.

Business interests. If you have an ownership interest in a business, such as a privately held corporation, limited liability company or partnership, it's likely possible to transfer your interest to your revocable trust while retaining voting rights and other powers. Check the company's bylaws or operating agreement to see if there are any approvals required or other restrictions on transfer.

What about life insurance policies?

It's possible to have your revocable trust hold an insurance policy on your life, but it's not necessary, since life insurance proceeds pass via beneficiary designation, thereby avoiding probate. It's more common to name your revocable trust as beneficiary of your life insurance policy so that the proceeds can be distributed according to the terms of your trust.

If you're concerned about asset protection or if your wealth is great enough that gift and estate taxes are an issue, it may be advisable to hold your life insurance policy in an irrevocable life insurance trust (ILIT). A properly designed ILIT allows the death benefit to bypass your taxable estate. And if the ILIT is named as beneficiary of the policy, it also offers some protection against creditor claims.

Personal property. For tangible personal property — such as furniture, artwork, antiques or collectibles — you can simply execute an assignment of personal property transferring ownership to your trust.

Assets that shouldn't be in your trust

Here are some assets you should keep out of your revocable trust:

Retirement accounts. Avoid transferring IRAs, 401(k) plans or other tax-advantaged retirement accounts to your revocable trust. Doing so may be considered a distribution, which can trigger income tax and early withdrawal penalties. A better approach is to allow the account to pass to your designated beneficiary. Another advantage of this approach is that it'll avoid probate. You can name your trust as a primary or secondary beneficiary of the retirement account but consult your advisor to discuss any tax implications of various beneficiary designations.

Health Savings Accounts (HSAs) and Medical Savings Accounts (MSAs). These accounts, which allow you to pay for qualified medical expenses with pre-tax dollars, are individual accounts that generally cannot be transferred to a trust. However, as with retirement accounts, you can name your revocable trust as a beneficiary of your HSA or MSA. Although, as with the discussion above relative to retirement accounts, whether you should depends on the specifics of your circumstances.

Vehicles. There are several reasons to keep automobiles and other vehicles out of your revocable trust. For one thing, tax and registration considerations can make transferring a vehicle to a trust cumbersome and/or expensive. And if you have an outstanding auto loan, the lender may not allow you to transfer title.

Another concern is that if the trust is the owner and the vehicle is involved in an accident, other trust assets could be exposed to liability claims. The tradeoff, of course, is that the vehicle may be subject to probate, although many states offer streamlined procedures for transferring certain vehicles to heirs outside of probate.

Have a backup plan

In case you neglect to transfer certain assets to your revocable trust, be sure that you have a "pour-over will," which automatically transfers any assets titled in your name to your trust. Ideally, you'll transfer all appropriate assets to your trust during your lifetime, but in case anything falls through the cracks, a pour-over will ensures that those assets are distributed according to the terms of your trust. Contact your estate planning advisor with questions involving revocable trusts.

Will contests don't happen only on TV

Take the proper steps to avoid family chaos after your death

If you watch enough drama-based television shows, you're likely to come across a scene where family members are gathered to hear the reading of a loved one's will after his or her death. Once finished, an heir stands up and starts shouting how he or she has been treated unfairly and plans to contest the will.

This occurs not only on TV or in the movies. It also happens in real life. Indeed, regardless of how harmonious your family may be during your life, there's always a chance that a disgruntled family member may challenge your estate plan after your death.

Contesting a will

Your last will and testament, if properly executed, is a road map for an executor to follow. Notably, it includes a legally enforceable mandate as to the distribution of your assets to named beneficiaries. Some bequests are specific, while others may be covered by the residuary clause.

> *The contest to a will is made in probate court by an "interested party."*

The contest to a will is made in probate court by an "interested party." To contest a will in any state, the person must have legal standing. This ability generally is restricted to beneficiaries named in the will, those who were named as beneficiaries in a prior will that have been cut out or that are receiving a reduced inheritance, and anyone else eligible under the state's intestacy laws. Typically, this means a spouse, child or other lineal descendant.

Beneficiaries can't contest a will until they've reached the age of majority in the state (age 18 in most states). However, a parent or guardian can initiate legal action on a younger beneficiary's behalf.

Understanding why wills are contested

There are several reasons for contesting a will:

Violation of state law. Each state has specific laws governing the wills of its residents. Generally, you must sign the will in the presence of at least two witnesses. All three people must be in the room watching each other sign the document. Depending on state law, other technicalities may have to be observed. Don't assume that the will is legally binding just because it was signed in your attorney's office.

Lack of competency. Did the testator (the person who made the will) have the capacity to understand the terms of the signed will? This is another aspect that's governed by state law. It's typically difficult to prove to the court that a testator lacked the requisite mental competency.

Undue influence. As people get older, they may be more susceptible to being influenced by others, sometimes resulting in revisions or even a complete rewrite of a will. The main issue is whether enough pressure was exerted on the testator to cause a loss of free will. For example, this may occur when the influencer isolates the testator from other family members and friends. Note that mere threats, nagging and verbal abuse usually aren't sufficient to uphold a challenge. As with a lack of capacity, this charge generally is difficult to prove under state law.

Fraud. Someone contesting a will may claim that the testator was duped into signing it. Let's say that the testator signs a different document, such as a living will relating to end-of-life decisions, and thinks that it's a last will and testament. This type of challenge often relates to mental competency. The testimony of witnesses can be significant in these cases.

A subsequent will. Did the executor probate the latest version of the will? A subsequent will revokes other versions. It's only the last one that counts as long as it meets state requirements. Frequently, a testator modifies or rewrites a will without notifying all the interested parties, leading to a challenge in court.

Taking proactive protection steps

Be proactive about protecting your estate from will contests. Start by observing all the legal technicalities in your state. Discuss the terms of your will and the reasons for your decisions with your loved ones so they won't be caught by surprise.

To avoid unexpected tax bills, adequately disclose your gifts

If you transfer business interests or other assets to your loved ones, the IRS generally has three years to challenge their value for gift tax purposes or to claim that a transfer you treated as a nongift was in fact a gift or partial gift. However, the three-year statute of limitations period doesn't begin to run until you "adequately disclose" the transfer to the IRS. Otherwise, the IRS can come after you for unpaid gift taxes, plus penalties and interest, years or even decades later.

To avoid this situation, your gift tax return must satisfy federal tax regulations' adequate disclosure requirements. And even if you treat a transfer as a nongift (such as the transfer of an asset in exchange for full and adequate consideration), you may want to report it on a gift tax return anyway to prevent the IRS from arguing, many years later, that you made a taxable gift.

Note that if you decide not to disclose the transaction on a gift tax return, it's crucial that the transaction is documented properly and

that the documentation is retained by you and the buyer.

What are the adequate disclosure requirements?

Generally, to adequately disclose a transfer, file a gift tax return for the year in which the transfer is completed, containing the following information:

- A description of the transferred property and any consideration received,
- The identity of, and relationship between, the transferor and each transferee,
- If property is transferred to a trust, the trust's tax identification number and a brief description of its terms (or a copy of the trust instrument),
- A detailed description of the method used to value the transferred property or a qualified appraisal, and
- A statement describing any position taken that's contrary to any proposed, temporary or final tax regulations or revenue rulings published at the time of the transfer.

Additional information is required for certain transactions between related parties, such as grantor retained annuity trusts, qualified personal residence trusts, and transfers of interests in corporations or partnerships.

For transfers reported on a gift tax return as non-gifts, describe the methods used to value the property or furnish an appraisal. You'll also need to explain why they're not gifts.

Substantial compliance is sufficient

Often, strict compliance with tax regulations is required. However, in a recent U.S. Tax Court case (*Schlapfer v. Commissioner*), the court held that substantial compliance with the adequate disclosure regulations is sufficient. However, the disclosure must be "sufficiently detailed to alert the Commissioner and his agents as to the nature of the transaction so that the decision as to whether to select the return for audit may be a reasonably informed one."

> *Generally, to adequately disclose a transfer, file a gift tax return for the year in which the transfer is completed.*

This decision provides some comfort to taxpayers who fail to cover all the bases when disclosing gifts. But to avoid an IRS challenge and potential litigation, it's advisable to follow the regs as closely as possible.

Protect your estate plan

Does your estate plan involve gifting assets to family members or others? Or is there a risk that a nongift transfer could later be characterized as a partial gift? The best way to protect your plan is to report the gift or transfer on a timely filed gift tax return that satisfies the adequate disclosure requirements. Doing so can help minimize the chances of unwelcome tax surprises years or even decades in the future. Contact your estate planning advisor for more details.

ESTATE PLANNING RED FLAG

You and your siblings have inherited your parents' home

It's not unusual for parents to leave their primary residence or vacation home to their children. Unless your parents' wills or trusts specify otherwise, you and your siblings will receive equal shares of the home, which may lead to conflicts if you have different financial needs or differing views about how the home should be used.

The first step is to sit down with your siblings and have an open, honest discussion about your wishes for handling the inherited home. Generally, the options are:

- Keep the home and share it among family members,
- Rent out the home and share the rental income,
- Sell the home and divide the profits, or
- Arrange for one sibling to buy out the others.

If you decide to share the home, have a written agreement drafted by your attorney that outlines rules regarding scheduling, allowable uses, and responsibility for maintenance and expenses. If you choose to sell the home or arrange a buyout, obtain a professional appraisal to avoid disputes over the home's value.

If you rent out the home, determine how you'll handle rent collection, maintenance and other rental activities. One option is to engage a property management company to handle the day-to-day management.

Another issue to consider is how the title to the property will be held. For example, if you and your siblings own the home as tenants in common, then your respective interests will pass to your heirs according to your individual estate plans. But if you hold the property as joint tenants, then when one sibling dies, the surviving siblings receive his or her share.

Legal Insight. Business Instinct. Community Impact.

Founded in 1925, the Shumaker team of more than 300 lawyers and advisors is a premier provider of legal and legislative solutions, focused on being a positive and impactful difference maker for our clients and in the communities we serve. Aligned with this mission, we are committed to understanding your business in order to provide the exact legal resources you need.

Our firm's presence in multiple states dramatically increases our ability to meet our clients' estate planning and estate administration needs. Shumaker attorneys are located across our 11 offices in Toledo, Columbus, and Akron, Ohio; Tampa, Sarasota, Tallahassee, and Dade City, Florida; Bloomington, Minnesota; Charleston and Greenville, South Carolina; and Charlotte, North Carolina. In total, we have attorneys licensed to practice in 26 states, the District of Columbia, Puerto Rico, and Ontario, Canada and have established relationships with partner firms in the other states to seamlessly manage transactions across state lines.

Wealth Strategies

Shumaker's Wealth Strategies Service Line focuses on all areas of personal succession, business succession, insurance, asset protection, and charitable giving planning to develop fully informed estate plans that meet the specific needs and wishes of individuals, families, and business owners. Our attorneys regularly advise high-net-worth individuals and business owners on estate planning strategies that maximize wealth preservation and minimize taxes on transfers to family members, charities, and other recipients. Recognizing the importance of a strong lawyer-client relationship, we work as strategic partners with our clients, allowing us to respond effectively to their evolving estate planning and estate administration objectives.

Since the complexities of estate planning can involve many areas of the law, we arrange for clients whose complex estate plans are impacted by tax, corporate, and pension planning issues to consult with firm colleagues in these areas in order to develop fully informed plans. Clients depend on our familiarity with all aspects of the estate planning and administration process, as well as with the latest planning tools and techniques, to help them achieve their goals.

SHUMAKER

We welcome the opportunity to discuss your situation and provide the services required to help you achieve your estate planning goals. Please call us today and let us know how we can be of assistance.

www.shumaker.com