THE ESTATE PLANNER

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Getting remarried?

Understand your spouse's inheritance rights

If you're getting remarried, you may have very different expectations than you did when you married the first time, especially when it comes to estate planning. For example, if you have children from a previous marriage, your priority may be to provide for them. You may feel that your new spouse should have more limited rights to your assets than those of your spouse in your first marriage.

Unfortunately, the law doesn't see it that way. In nearly every state, a person's spouse has certain property rights that apply regardless of the terms of the estate plan. And these rights are the same, whether it's your first marriage or your second or third. Here's an introduction to spousal rights and some of the strategies you may be able to use to limit them.

State law is key

Spousal property rights are creatures of state law, so it's critical to familiarize yourself with the laws in your state to achieve your planning objectives. Most states provide a surviving spouse with an "elective share" of the deceased spouse's estate, regardless of the terms of his or her will or certain other documents. The remaining states (except Georgia) are community property states. This article focuses on elective share states, but similar planning strategies may be available in community property states as well. (See "What about community property?" on page 3.)

Generally, a surviving spouse's elective share ranges from 30% to 50%, though some states start lower and provide for progressively larger shares as the duration of the marriage increases. Perhaps the most significant variable, with respect to planning, is the definition of assets subject to the surviving spouse's elective share rights.

In some states, the elective share applies only to the "probate estate" — generally, assets held in the deceased spouse's name alone that don't have a beneficiary designation. In other states, it applies to the "augmented estate," which is the probate estate plus certain nonprobate assets, such as one or more of the following:

- Revocable trusts,
- Life insurance policies,
- Retirement or financial accounts that pass according to a beneficiary designation or transfer-on-death designation,

What about community property?

Community property states take a different approach to protecting a surviving spouse's interests. Rather than provide the spouse with an elective share of the deceased spouse's assets, community property laws generally give each spouse an undivided one-half interest in all money earned and property acquired during marriage, regardless of how it's titled. Certain exceptions exist.

In other words, there's no need to give the surviving spouse the ability to override the terms of the deceased spouse's estate plan, because the deceased spouse lacks the power to dispose of the surviving spouse's half of the community property.

As in elective share states, there may be strategies to limit the surviving spouse's rights to marital property. For example, the surviving spouse can waive his or her rights to them in a prenuptial or postnuptial agreement.

- Jointly owned assets that pass automatically to a joint owner, and
- Lifetime gifts made during a specified "lookback" period (for example, one year) prior to death.

By developing an understanding of how elective share laws apply in your state, you can identify potential strategies for bypassing them.

Planning strategies

Elective shares are designed to protect surviving spouses from being disinherited. But there may be good reasons for limiting the amount of property that goes to your spouse when you die. For one thing, your spouse may possess substantial wealth in his or her own name. And you may want most of your estate to go to your children from a previous marriage. Or perhaps the bulk of your wealth is tied up in a family business that you want to keep in the family.

Strategies for minimizing the impact of your spouse's elective share on your estate plan include:

Making lifetime gifts. By transferring property to your children or other loved ones during life (either outright or through an irrevocable trust), you remove those assets from your probate estate and place them beyond the reach of your surviving spouse's elective share. If your state uses an augmented estate to determine a spouse's elective share, lifetime gifts will be protected so long as they're made before the lookback period or, if permitted, your spouse waives the lookback period.

Transferring assets to a revocable trust. In most (but not all) probate-only states, transferring assets to a revocable trust is sufficient to shield them from your spouse's elective share. In augmented estate jurisdictions, the elective share generally applies to revocable trusts. However, the laws of some states provide that the augmented estate only includes assets transferred to a revocable trust *during marriage*. In that case, it may be possible to protect assets from the elective share by transferring them to a revocable trust *before* remarrying.

Purchasing life insurance. Life insurance can be a great way to create wealth and liquidity for your children or other family members, and in probate-only states it's generally shielded from your spouse's elective share. Augmented estates usually include life insurance, but in some states, it may be possible

to exclude it by holding it in an irrevocable life insurance trust.

Retitling assets. In probate-only states, you may be able to protect assets by holding them jointly with a child or other family member with right of survivorship.

Having your spouse sign a waiver. One thing most elective share states agree on is that your spouse can waive his or her elective share in writing, either through a standalone waiver or as part of a broader prenuptial or postnuptial agreement.

Check beneficiary designations on retirement plans and other accounts and be sure that they name your children or other intended beneficiaries. Keep in mind that changing certain beneficiary designations requires your spouse's consent.

Get professional help

State elective share laws are complex and can vary dramatically from state to state. If you're remarrying, consult your estate planning advisor to evaluate their impact on your estate plan and explore strategies for protecting your assets. ▮

Estate planning vocab 101: Executors and trustees

Among the many decisions you'll have to make as your estate plan is being drafted is who'll you appoint as the executor of your estate and the trustee of your trusts. These are important appointments, and, in fact, both roles can be filled by the same person. Let's take a closer look at the duties of an executor and a trustee.

Duties of an executor

The executor (called a "personal representative" in some states) is the person named in a will to carry out the wishes of the deceased. Typically, the executor shepherds the will through the probate process, takes steps to protect the estate's assets, distributes property to beneficiaries according to the will, and pays the estate's debts and taxes.

Most assets must pass through probate before they can be distributed to beneficiaries. (Note, however, that assets transferred to a living trust are exempted from probate.) When the will is offered for probate, the executor will also obtain "letters testamentary" from the court, authorizing him or her to act on the estate's behalf.

> *It's the executor's responsibility to locate, manage and disburse the assets of the estate.*

It's the executor's responsibility to locate, manage and disburse the estate's assets. In addition, he or she must determine the value of property. Depending on the finances, assets may have to be liquidated to pay debts of the estate.

Also, the executor can use estate funds to pay for funeral and burial expenses if no other arrangements have been made. The executor will obtain

copies of the death certificate, which will be needed for several purposes, including closing financial accounts, canceling certain benefit payments and filing the final tax return.

So, whom should you choose as the executor of your estate? Your first inclination may be to name a family member or a trusted friend. But this can cause complications.

For starters, the person may be too grief-stricken to function effectively. And, if the executor stands to gain from the will, there may be conflicts of interest that can trigger contests of your will or other disputes by disgruntled family members. Furthermore, the executor may lack the financial acumen needed for this position. Frequently, a professional advisor whom you know and trust is a good alternative.

Duties of a trustee

The trustee is the person who has legal responsibility for administering a trust on behalf of the trust's beneficiaries. Depending on the trust terms, this authority may be broad or limited.

Generally, trustees must meet fiduciary duties to the beneficiaries of the trust. They must manage the trust prudently and treat all beneficiaries fairly and impartially. This can be more difficult than it sounds because beneficiaries may have competing interests. The trustee must balance out their needs when making investment decisions.

The decision about naming a trustee is similar to the dilemma of choosing an executor. The responsibilities require great attention to detail, financial acumen and dedication. Because of the heavy reliance on investment expertise, choosing a professional over a family member or friend is generally recommended.

At the very least, make it clear to the trustee that he or she may — and should — rely on professionals as appropriate.

Designating alternates

An executor can renounce the right to this position by filing a written declaration with the probate court. Along the same lines, a designated trustee may decline to accept the position or subsequently resign if permission is allowed by the trust or permitted by a court. This further accentuates the need to name backups for these important positions.

Without a named successor in the executor role, the probate court will appoint one for the estate. For a trustee, the trust will often outline procedures to follow. As a last resort, a court will appoint someone else to do the job.

Making your decisions

Before you begin planning your estate, it's worth your while to brush up on basic estate planning terms. It's especially critical to learn the roles of an executor and a trustee because you'll have to make decisions on who you want to fulfill those appointments. Contact your estate planning advisor with questions. ▮

Should you file a joint tax return for the year of death?

The death of a spouse is a devastating, traumatic experience, and if it happens, dealing with taxes and other financial and legal obligations are probably the last things on your mind. Unfortunately, many of these obligations can't wait and must be addressed in the months to follow. One important issue for the surviving spouse to consider is whether to file a joint or separate tax return for the year of death.

Final tax return

When someone dies, his or her personal representative is responsible for filing an income tax return for the year of death (as well as any unfiled returns for previous years). For purposes of the final return, the tax year generally begins on January 1 and ends on the date of death. The return is due by April 15 of the following calendar year.

Income that's included on the final return is determined according to the deceased's usual tax accounting method. So, for example, if he or she used the cash method, the income tax return would only report income actually or constructively received before death and only deduct expenses paid before death. Income and expenses after death are reported on an estate tax return.

The surviving spouse, together with the personal representative, may file a joint return. And the surviving spouse alone can elect to file a joint return if a personal representative hasn't yet been appointed by the filing due date. (However, a court-appointed personal representative may later revoke that election.)

Pros and cons of a joint return

In the year of death, the surviving spouse is generally deemed to be married for the entire calendar year, so he or she can file a joint return with the estate's cooperation. If a joint return is filed, it'll include the deceased's income and deductions from the beginning of the tax year to the date of death, and the surviving spouse's income and deductions for the entire tax year.

Possible advantages of filing a joint return include:

- Depending on your income and certain other factors, you may enjoy a lower tax rate.
- Certain tax credits are larger on a joint return or are unavailable to married taxpayers filing separately.
- IRA contribution limits, as well as the amount allowed as a deduction, may be higher for joint filers.

There may also be disadvantages to filing jointly. For example, higher adjusted gross income (AGI) may reduce the tax benefits of expenses, such as

medical bills, that are deductible only to the extent that they exceed a certain percentage of AGI.

Crunch the numbers

To determine the best approach, ask your tax advisor to calculate tax liability based on both joint and separate returns. While married filing separately might be the only option available to you, other possibilities — depending on the facts — include qualifying widow(er) and head of household. ∎

ESTATE PLANNING RED FLAG

You named your child or grandchild as beneficiary of your IRA

If you have a traditional IRA that designates your child or grandchild as beneficiary, be sure to consider the potential tax impact of the SECURE Act, which took effect in 2020. Previously, if you named someone other than your spouse as beneficiary, the recipient would have the ability to spread distributions over his or her life expectancy. He or she could then maximize tax-free growth while deferring, and often reducing, income taxes on distributions.

The SECURE Act limited the benefits of these so called "stretch IRAs." Now, nonspousal inherited IRAs must be distributed to beneficiaries within 10 years (with certain exceptions).

This is not to say that naming a child or grandchild as beneficiary is a mistake. In many cases, they may be the most desirable recipients of your wealth, regardless of the 10-year distribution requirement. But if you chose your beneficiary before the SECURE Act was passed, you may want to consider alternatives that can reduce the tax impact on your family.

If you wish to defer distributions (and taxes) as long as possible, consider naming your spouse as beneficiary. Spouses still have the ability to take distributions over their life expectancies, or to roll over an inherited IRA into their own IRA and — presuming your spouse didn't reach age 70½ before 2020 — defer distributions until they reach age 72.

If your spouse isn't a beneficiary option, there are strategies you can use to achieve similar benefits to a stretch IRA. For example, you might leave your IRA to a charitable remainder trust (CRT) that makes payments to your child for life with the remainder going to charity.

Because a CRT is a tax-exempt entity, taxes are deferred until funds are distributed to a noncharitable beneficiary, so the benefits are similar to those provided by a stretch IRA. Of course, you'll need to weigh those benefits against the cost of setting up the trust and leaving a portion of the funds to charity.

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