FPSB® GLOBAL EDUCATION PROGRAM

RISK AND ESTATE PLANNING SPECIALIST

MODULE

Estate Planning

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FINANCIAL PLANNING
STANDARDS BOARD

Estate Planning

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Introduction

Imagine asking someone on his death bed how he would like to be remembered and getting the response: "As a person who had an estate plan that saved taxes" (Diliberto, 2006, p. 105).

Taxation, while an important part of many estate-planning scenarios, does not define the topic. Instead, estate planning looks at how an individual wants to address the end of his or her life. Postmortem (i.e., after death) estate (property/wealth) distribution is a significant planning focus, but even that is not the sole estate planning target. Further, even though estate planning may prepare for the end of life, a lot of the planning and plan execution happens much earlier. We will explore these matters in more detail in this course.

What is an Estate?

All the assets a person owns make up his or her estate. Assets may include securities, real estate, business interests, physical possessions, cash, titles, intellectual property, and any other items a person may own (Downes, 2010, p. loc 5753). While much of financial planning targets asset accumulation and management, estate planning focuses more on managed distribution.

The list of items in a person's estate can be expansive, and may include such items as:

- Primary residence
- Secondary, vacation, or other dwellings
- Home furnishings, furniture, appliances, and other household items
- Clothing
- Jewelry
- Cameras, computers, and sound equipment
- Sports and recreational equipment
- Cars and other vehicles
- Cash, banking and securities accounts, notes and structured payments
- Life insurance policies (and sometimes other policy types)
- Vested pensions and other retirement plan assets
- Intellectual property (e.g., authored works, copyrights, trademarks, etc.)
- Royalties and other income streams

We could continue to expand the list, because a person's estate includes everything he or she owns or has a contractual right to receive. The primary implication here is that even people who feel they have little or no estate probably have more than they think.

Some of the property that gets included in a person's estate depends on how it is titled. As with most areas in this estate planning course, titling implications vary considerably by territory. As an example, consider the treatment of marital/matrimonial property. Some territories consider each spouse's property to belong only to that person. A husband's property belongs to the husband and a wife's property belongs to the wife. As a result, neither spouse's property would be included in the other's estate. However, more often, marital property is considered to be shared property. That is, each spouse owns marital assets jointly (in some fashion). Marital assets may be divided evenly or by some other formula. In some cases, neither spouse can unilaterally distribute marital property. So, a wife who wants to give a piece of property to a daughter from a prior marriage may not be allowed to do so without express permission from her husband; a husband who wants to make a substantial donation to a charity has to get his wife's approval. In territories where each spouse owns all or part of his or her assets, the wife might have no difficulty giving the property to her daughter, or the husband to the charity.

Further, property one spouse owns prior to the marriage may be treated differently than property either spouse purchases within the marriage.

For purposes of this course, we cannot make very many assumptions as to the implications of how property is owned, titled, and distributed. Every financial planner will have to become familiar with the laws and practices in his or her territory (and/or jurisdiction within a territory if applicable). We should note one additional caution: If an individual, married couple, or unmarried/cohabiting partners move from one territory to another, the laws of ownership and distribution may be different than those in their prior territory. Most often, the new laws will have some effect on jointly held property. In many cases, property owned prior to the move is treated according to the laws and practices of that territory, but not always. Further, when considering cohabiting partners (i.e., not married, but living together), ownership and distribution rules can vary substantially from one territory to another[1].

[1] For ease of writing, we will normally consider civil partnerships (cohabiting, unmarried adults) to follow the same general rules as if married. However, this certainly is not always the case, and the financial planner must understand the treatment of civil partnerships and how it may differ from the treatment of those who are married. Territories also treat separation, divorce, and remarriage in different ways, and the financial planner needs to be aware of the rules and practices in his or her territory.

Chapter 1:

Learning Objectives

Upon completion of this section, students should be able to:

1-1 Describe estate planning and wealth distribution terms

Topics

Terms and Descriptions

The financial planning component areas generally have their own terminology. Investment planning and asset management includes terms such as fundamental analysis, standard deviation, risk profile, modern portfolio theory, and the like. Risk management and insurance planning has terms such as mortality risk, law of large numbers, preexisting conditions, and many more. Estate planning is no different, having unique terms and those used elsewhere that are applied in specific ways. We will explore some estate planning terms in this chapter.

Before doing so, you should understand that there is no good way for this course to fully incorporate all terms in use in all territories. Nor will it be possible to correctly identify how such terms are applied in each locale. We have issued this caution in prior courses, and it is perhaps even more applicable to estate planning. It is unlikely that most financial planners also will be estate planning legal experts. The nuances of national and perhaps regional/jurisdictional laws go far beyond the typical financial planner's expertise. At some point, estate planning often requires a legal background and licensing. As such, while it is important for financial planning professionals to be familiar with this content, it is equally important to understand the need to avoid the unauthorized practice of law and to partner with a competent estate planning professional (e.g., lawyer). Know when to make a referral to remain in compliance with applicable laws and regulations, and to provide the highest degree of service to your clients. That said, let's begin looking at estate planning terminology.

Estate Planning and Inheritance

An **estate,** for our purposes, is all rights, titles, and interests a person has in any property. It also includes all debts and liabilities. The person may be living or dead, and the term encompasses all owned property prior to death and distribution of that property. This immediately raises the question "What is property?" We can use several terms to define property, among which are the following:

- **Real:** This refers to the land and permanent (immovable) structures on it. This is sometimes called *real estate* and at other times referred to as *immovable property*. Although there are technical differences between the terms, we will refer to real estate or real property as the overall term.
- **Personal:** Personal property may either be *tangible* or *intangible*. Tangible personal property refers to items, other than real property, that has a physical presence (i.e., can be touched) and has value. Intangible personal property is that which is other than real or tangible. This is property, such as securities, bank notes, and intellectual property (although this sometimes is considered as being in its own category) that has value as a

result of legal, contractual rights. Securities sometimes also may be considered as having their own category.

- **Community:** Several states and a few territories (e.g., France, Brazil, U.S.) have a category of property ownership between spouses known as *community property*. Specific regulations differ, but generally, community property is all property acquired and held as part of the matrimonial estate. Within community property regimes, some property may be excluded or exempt.

Estate planning is the process of developing strategies to achieve goals relating to management and distribution of property in such a way as to efficiently accomplish tax and nontax goals. Estate planning focuses on distribution when the owner has died, and also encompasses plans and distribution while he or she is living. Estate planning also integrates decisions around health care and incapacity. All of this should be done long before the property owner's death so that, at death, property distribution will happen in the way the decedent (deceased property owner) desired.

Inheritance is the receipt of property from an estate, often as a result of estate planning. It can include taking physical ownership of real and tangible property. It also may involve receiving legal and/or beneficial ownership of intangible property. This includes all rights, interests, and titles in the property. Legal ownership refers to the right to manage property, including the ability to transfer it from one person or entity to another. Beneficial (or equitable) ownership is the right to use and enjoy property. An individual may have one or both types of ownership, with heirs (i.e., those who inherit property as outright owners) having both.

- *Present interest* refers to legal or beneficial ownership that allows a person to use the property immediately. In addition to situations where a person has outright (current) ownership, beneficiaries of a trust who receive current income from the trust (or can demand payments) are said to have a present interest in the trust assets.
- *Future interest* is used when a person will have ownership eventually but cannot use the property immediately. Beneficiaries in a will have a future interest in the property, because they must wait until the testator (i.e., person making a will) dies before they inherit the property. Trust beneficiaries who receive trust assets after income from the trust terminates are said to have a future interest. A trust beneficiary who receives mandatory income payments (or can demand those payments) as well as ultimately receiving the trust assets (i.e., corpus) has both a present and future interest.

Present and Future Interest Example. Estelle's mother has given her a car to drive. The car has been retitled in Estelle's name and she now has full ownership. Estelle has a present interest in the car.

Estelle's father has named her in his will as an heir to his estate. She is going to inherit 50% of her father's property, but she must wait to receive any of it until his will becomes active at his death. Estelle has a future interest in the property to be provided by her father's will.

Taxation is one of the major aspects of estate planning, and territories may tax the estate, the heir (i.e., inheritor), or both. Further, the territory or jurisdiction[2] may have different tax

[2] For our purposes, a "territory" refers to a nation. A jurisdiction is a subdivision or state within the territory. For example, Belgium is a territory. Within Belgium are three distinct jurisdictions: Brussels capital region, the Flemish region, and the Walloon region. Jurisdictions often have rules and regulations that differ from those of the territory. Further, *jurisdiction* may refer to rules and laws applicable within a territory. *Jurisdiction* also may refer to having legal authority in a territory or smaller area within the territory.

structures, exemptions, inclusions, ownership and distribution requirements, etc. Some territories also tax wealth as part of the distribution of assets. Unless it is material to understanding the content, we will refer to estate planning and taxation of the estate and mean it to include the other options. At this point it will be good to remember that either the estate, the inheritor, or both may be taxed, and one part of estate planning involves attempting to limit those taxes. Wealth transfer tax, especially on real estate, may be referred to as stamp tax or duty in some territories. For our purposes, we will include stamp duty as being part of overall estate taxes.

Law: Common and Civil

There are two primary legal systems in the world. Common law, also known as English common law, is a legal system based on the common law courts of England. The legal system found in most British Commonwealth (i.e., the Commonwealth) states (e.g., Australia, the Bahamas, Canada, Fiji, Malaysia, Malta, New Zealand, United Kingdom, and others) and the United States generally follow case law and precedent (with exceptions) going back to England over hundreds of years, and to some degree, based on laws dating from the Middle Ages.

Civil law dates back to Roman times and is embraced by many European and Scandinavian countries, especially France and Germany, as well as Bulgaria, Egypt, Brazil, Chile and several other Central and South American territories, and others. While it's not important to know all about the two legal systems, you should recognize that territories in each system address estate planning in different ways. Civil law tends to be more prescriptive than common law. That is, it applies a greater amount of laws with specific steps and application. Common law, in general, allows a little more flexibility in interpretation and application of relevant regulations. Civil law tends to more specifically identify things such as who can inherit, laws of succession, compulsory/forced heirs, and the like.

There are similarities between the two systems, as well as quite a few differences. One major difference relates to the use of trusts. Common law generally recognizes trusts, while civil law may not. A number of territories have agreed to abide by the Hague Convention (HCCH) of 1 July 1985 on the Law Applicable to Trusts and on their Recognition, which entered into force 1 January 1992 (HCCH, 1992)[3]. By doing this they have agreed to accept the use of trusts in one form or another. We will look at trusts in a later chapter.

Sharia

Sharia, also known as Islamic law, is applied to governance of most Muslim territories (in addition to or in lieu of civil or common law). Sharia stands apart from both common and civil law and is primarily derived from teachings found in the Quran and the Sunna—the sayings, practices, and teachings of the Prophet Mohammed (Johnson & Aly Sergie, 2014). The course will refer to Sharia occasionally as applicable and will primarily focus on common and civil law.

Legal Documents and Distribution Methods

Estate planning has a primary focus on managing and distributing assets according to the wishes of the property owner. Over time, several laws and methods have been developed to oversee this process

[3] Member territories that have signed, ratified, or agreed to this law as of 26 October 2017 include: Australia, Canada, China (Hong Kong only), Cyprus, France, Italy, Luxembourg, Malta, Monaco, Netherlands, Norway, Panama, Switzerland, UK, U.S.

Probate is the process of settling a decedent's estate. When an individual dies the estate must go through the probate process, except for those assets that pass by law or will substitute/contract. Essentially, probate is a legal proceeding in which a decedent's will is reviewed by a court (e.g., probate court) which has legal authority over the settlement of the decedent's estate. The court determines the legality of the will and arranges for whomever and whatever may be necessary to carry out terms of the will (Barrow, 2017, p. loc 253). In cases where there is no will, or one does not apply (e.g., mandatory succession rules), the estate will be settled according to intestate succession rules. Generally, life insurance assets and other contracts that include a named (nominated) beneficiary pass outside the normal probate process. While the probate process is likely to incur expenses and will help identify taxable property, the probate estate is not identical to the taxable estate. Probate therefore refers to the settlement process rather than the determination of applicable taxes. Also note that not every territory requires a will to pass through a formal probate process (but most do).

Probate estate includes all items that are included in the probate process (e.g., that pass to heirs via a decedent's will or a territory's intestacy statutes).

A **will** is a document (except in cases of a valid oral [nuncupative] will) that specifies how the property owner wants his or her estate to be distributed at death. It can be used to identify someone to administer the estate (i.e., executor or personal representative) and identify a guardian/administrator for minor children. A will normally cannot be used to override applicable laws or will-substitute contracts. A will may be legal/formal (i.e., written following applicable regulations), properly witnessed, notarized when required, and approved by an authorized individual or entity.

Wills, where allowed, may be handwritten or oral. A territory may or may not honor either type of will. To be valid, a handwritten will must be complete, signed, and include a creation date. Generally, a handwritten (holographic) will must be delivered to an authorized person, such as a notary or justice of the peace. Oral wills are seldom allowed and, when used, must be heard by witnesses (usually at least two).

A will may be testamentary or *inter vivos* (living). A testamentary will is one that comes into effect upon the death of the will maker. The person making the will may be known as the *testator*. A variant of that term is used to identify when an individual dies without having executed a valid will. He or she is identified as dying *intestate*. A will can be quite simple or complex. A simple will may direct that all the decedent's assets be passed to his or her spouse. This type of will would not be valid in territories where succession laws mandate primary estate division among the children in addition to, or in lieu of, the spouse. As a result of this and other scenarios, a will may require a more complex structure. To be legal, a will must be written in legal form for the territory in which the individual is domiciled. This means a perfectly legal will in one territory may need to be rewritten when the individual moves to another territory (or sometimes, state or other political subdivision within the territory).

Even a simple will is likely to be more complex than just stating some variant of, "divide my assets among my spouse and children." To be valid, most wills include statements identifying how debts are to be handled. Then, the testator might want to identify the percentages of property that is to go to each heir (e.g., spouse, children, etc.). As a will becomes more complex, it might include authority to send assets into a trust or include one or more charitable organizations in the distribution. Depending on the territory, the testator may want the will to comply with certain laws designed to limit taxes and/or facilitate property distribution.

Sometimes trusts may be used to aid this function. Somewhere in the language of the will, there must be a statement of compliance with all relevant laws and regulations. Further, a will should be current. This means a will executed 30 years ago, when the individual had no children and few assets, will almost certainly need to be revised and rewritten to reflect current status. We will look at items to evaluate when reviewing a will in a later chapter.

An ***inter vivos*/living will** or **advance directive** is not meant to become applicable at the death of the testator. Instead, the document is a living will, one that is meant to be in force during the life of the maker. A living will fits in the broader category of advance directives, which may include powers of attorney, health care proxies, health care directives, and advance health directive (and may go by other titles). Some territories give this type of document full legal status. In others, it is used more to provide guidance regarding the individual's desires but does not have actual legal status. Some territories do not recognize the validity of this type of document at all.

The primary function of a living will (and alternatives) is to specify the course of treatment health care providers and caregivers should follow. It becomes especially useful in situations where the maker is incapacitated, and therefore unable to give personal guidance regarding what he or she wants to happen. A power of attorney (general, durable/enduring, springing, health care, physician's directive, etc.) is used to give an authorized representative power to act on behalf of the individual. The reason for all the terms in the parentheses is that a typical power of attorney terminates when the individual becomes mentally incapacitated (MLC, 2017). As is always the case, different territories do or do not honor these documents, and when they are honored, they must be in a compliant form for each territory. The HCCH enacted the *Convention on the International Protection of Adults* in January 2000[4]. This document is somewhat broader than living wills in its application, and includes representation in business arrangements, but it does address situations in which one person may give another authority to represent him or her in the event of incapacity. We will explore this type of document more fully in Chapter 5, Planning for Incapacity.

Living Will—Advance Directive (PARTIAL SAMPLE)
Medical Durable Power of Attorney I, Sample Person, hereby appoint: Authorized Representative, living at 1234 Main Street Anytown as my agent to make health care decisions for me if and when I do not have the capacity to make my own health care decisions. This gives my agent the power to consent to giving, withholding, or stopping any health care, treatment, service, or diagnostic procedure. My agent also has the authority to talk with health care personnel about my condition, access my medical records, get information, and sign forms necessary to carry out those decisions. If the person named as my agent is not available or is unable or unwilling to act as my agent, then I appoint the following person(s) to serve in the order listed below: Alternative One, 6578 Second Street, Anytown Alternative Two, 9123 Third Street, Anytown

[4] https://assets.hcch.net/docs/c2b94b6b-c54e-4886-ae9f-c5bbef93b8f3.pdf. As of 13 March 2017, the following member territories have signed, accepted, or ratified the document: Cyprus, Czech Republic, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Monaco, Netherlands, Poland, Switzerland, and UK. Some of the territories have formally identified reservations to the document. Being a signatory does not guarantee the convention is in place in the territory.

By this document I intend to create a Medical Durable Power of Attorney which shall take effect upon my incapacity to make my own health care decisions and shall continue during that incapacity.

http://www.caringinfo.org/i4a/pages/index.cfm?pageid=3289

Will substitutes are contracts that pass assets directly to a named beneficiary. Probably the most common and well-recognized such document is a life insurance contract. Most, if not all, territories consider life insurance contracts to be in a separate category. In many scenarios, proceeds from a life insurance policy are not considered part of the estate and pass outside probate and other succession laws directly to the named (or nominated) beneficiary. This is true in most cases, but not all. If there is no named beneficiary, proceeds probably will be pulled into the estate and may become subject to the probate process. Some territories do not apply estate/inheritance tax or income tax to the proceeds paid to a beneficiary. However, non-spousal beneficiaries may be taxed, corporations may be taxed, and perhaps there will be taxation in other situations. Some of the calculations to determine taxability can become rather complicated, depending in large part on the relationship of the beneficiary to the decedent. In some territories (e.g., France), life insurance may be used to bypass civil rules governing succession, thereby allowing assets to be passed to a broader array of individuals. Other types of contracts may or may not support distribution of assets outside of probate. Some of the status will depend on relevant tax treaties between territories. As always, check laws and regulations in your territory before acting or making recommendations.

Property Ownership

Property may be owned in a number of ways. It may be owned by an individual, spouses, multiple non-spouse individuals, organizations, trusts, partnerships, outright, with a mortgage, or with a life interest, among other options[5]. The way in which property is owned and titled often has an impact on how it is handled for estate planning purposes. This can apply to all property and especially to real property (e.g., real estate), such as a family home.

The simplest form of property ownership is individual ownership. Full and complete ownership often is identified as **fee simple** property ownership (sometimes also known as a *freehold*). One individual and no one else is involved. At death, such property will, of necessity, require direction from the decedent via a will or a mandate by the territory to determine its disposition. A mandate can come in two primary ways. The first is to distribute the property according to succession rules or forced heirship. It's possible for this to result in the spouse of the decedent taking full ownership of the property, or it may result in the children receiving ownership, or perhaps a combination of the two. Depending on the territory, property ownership may legally pass to the children, but the spouse will be entitled to use and enjoy the property while living. The second method (or mandate) is similar to succession and is known as the *rules of intestacy*. Intestacy is the result of the individual dying without a valid/legal will. When this happens, the territory (or state) will distribute the property according to its preexisting intestacy rules. The way in which intestacy rules work is very similar to rules of succession. The spouse often takes a primary position, but sometimes children are moved to the head of the line, perhaps in a shared arrangement with the spouse. In both cases, if property cannot be distributed to the immediate family, there is a line of succession that will be followed (e.g., siblings, cousins, parents, etc.).

[5] Note that foreign ownership of real estate is prohibited in many territories. In lieu of ownership, some territories allow foreigners to have a leasehold interest for a period of years. We will not refer to this type of arrangement, although a leasehold interest may pass from a decedent to an heir in some situations and would be considered to be part of the decedent's estate. Also note that in some territories, no one is allowed fee simple (or direct) ownership of real estate. The land belongs to the people and is administered by the state. In such situations, citizens are allowed a leasehold interest, and foreigners are not usually allowed to own property.

When more than one person holds property, the arrangement can have several different forms of ownership. Each type will result in different handling for estate distribution purposes. Joint ownership (also co-ownership, shared ownership, or concurrent ownership) typically has two primary forms: joint tenancy and tenants in common. Neither form requires ownership to be between spouses, although spouses often hold property as joint tenants. When spouses jointly own property they may do so using a form of joint tenancy with rights of survivorship known as **tenants by the entirety**. This arrangement is only available to spouses and, like other forms of joint ownership that have rights of survivorship, causes the property to pass from the decedent to remaining owner automatically, without passing through probate. Another way of saying this is that each owner has an equal right to the entire property.

Joint tenants own property equally, unless the owners hold the property as tenants in common (see below). At the death of one owner, that owner's share of the property will pass to the other owner(s). This arrangement, along with tenants by the entirety, cannot be superseded by a will. As such, the arrangement may be known as a will substitute. None of the joint tenant owners own an individual share of the property. Each owns all of the property. You may see joint tenants amended by adding *with rights of survivorship*. This amendment normally is only used to clarify the intent that property pass from one joint owner to the other(s) and is not a *tenants in common* arrangement.

Tenants in common may own property in unequal (proportionate) shares. Further, these owners may distribute their share of the property in any fashion they desire, without agreement by remaining owners. This arrangement does not come with rights of survivorship. As such, when one owner dies, his or her portion of the property passes to the decedent's estate and will be distributed according to the terms of the will. The remaining owners have no automatic right to the decedent's share of the property.

As is typical, each of the property ownership forms may have additional names and be addressed variously in different territories. Also, your territory may have subsets of one or more of the ownership options. One such is a *Strata*. A Strata is a form of ownership that allows an individual to hold title to part of a property, combined with shared ownership in the remainder (common property)[6]. If you are familiar with condominium or apartment ownership, it is a type of strata arrangement. For estate planning purposes, the property owner only has the right to distribute his or her share of the property, not any of the community or common property.

Tenants in Common Example. Ted, Ahmad, Jonas, and Fredrick want to purchase a holiday home together. The friends have known each other since their university days and want to get a place that will allow them to share holidays together with their families. The four have located a house they want to purchase, and they are trying to decide the best form of ownership. The total cost for the house is $200,000. Ted plans to invest $50,000. Ahmad will invest $30,000. Jonas plans to use the house more than the others and will invest $80,000. Fredrick plans to invest the remaining $40,000. After seeking professional legal and financial advice, the friends have decided to purchase the holiday home and title it as tenants in common. This will allow each of them to own the house in unequal (proportionate) shares relating to the investment each one will make. Ted will own 25%, Ahmad will own 15%, Jonas will own 40%, and Fredrick will own 20%. This arrangement will also allow each of the friends to sell his share of the house to the others or to someone else if the time ever comes they want to change the arrangement.

[6] https://www.strata.community/understandingstrata/what-is-strata

Community property, or marital property, where recognized, is all property acquired and held as part of the matrimonial estate (including debts). This has implications for estate planning, and also while spouses are living. Community property is all property, unless otherwise declared as being separate, that is acquired after marriage. Inherited property and property that each partner brings into the marriage is not automatically considered to be community property[7]. While living, each spouse may act, and the action will be considered part of the community property. This means a debt incurred by one partner becomes a debt owed by both. Property purchased by one becomes owned by both. For tax purposes, community property is treated variously depending on the territory (or state). For estate distribution purposes, some community property states/territories treat property in the same manner as tenants by the entirety. That is, all property becomes property of the remaining spouse. However, this is not always the case. In some situations and territories children may take priority and the surviving spouse may only receive a portion of the property. This may be modified by making legal arrangements prior to the decedent's death, but absent those arrangements, the surviving spouse may be disappointed.

Example 1		
Question		Susan, Jessica, Violet, and Helen want to purchase a holiday home together. The friends have known each other since their university days and want to get a place that will allow them to share holidays together with their families. The four have located a house they want to purchase, and they are trying to decide the best form of ownership. The total cost for the house is $400,000. Susan plans to invest $100,000. Jessica will invest $100,000. Violet plans to use the house more than the others and will invest $125,000. Helen plans to invest the remaining $75,000. After seeking professional legal and financial advice, the friends have decided to purchase the holiday home and title it as tenants in common. Which of the following statements is most likely correct?
	A.	If Susan dies, the remaining owners have automatic right to the decedent's share of the property.
	B.	If Susan dies, the remaining owners have no automatic right to the decedent's share of the property.
	C.	Susan will own 25%, Jessica will own 25%, Violet will own 25%, and Helen will own 25%.
	D.	Susan will own 25%, Jessica will own 25%, Violet will own 18.75%, and Helen will own 31.25%.
Correct Answer		**B.**

[7] However, even this is not standardized. For example, in South Africa, the standard marriage arrangement is for marital property to be known as community of property and includes everything owned or owed by either partner before and during the marriage. This can be amended, and there is another option that can be chosen, but community of property is the standard/automatic option (http://www.lawforwomen.co.za/legal-services/marriage/in-community-of-property.html).

Explanation		This arrangement does not come with rights of survivorship. As such, when one owner dies, his or her portion of the property passes to the decedent's estate and will be distributed according to the terms of the will. If Susan dies, the remaining owners have no automatic right to the decedent's share of the property.
Distractor #1	**A.**	This arrangement does not come with rights of survivorship. As such, when one owner dies, his or her portion of the property passes to the decedent's estate and will be distributed according to the terms of the will. If Susan dies, the remaining owners have no automatic right to the decedent's share of the property.
Distractor #2	**C.**	Susan will own 25%, Jessica will own 25%, Violet will own 31.25%, and Helen will own 18.75%.
Distractor #3	**D.**	Susan will own 25%, Jessica will own 25%, Violet will own 31.25%, and Helen will own 18.75%.

Laws of Succession and Forced Heirship

Technically, this comes under the category of distribution methods. However, for our purposes, it deserves a separate section, especially because of its estate planning impact. Many territories—especially those in primarily civil law jurisdictions such as Europe, Japan, Latin America, Russia, and many Islamic territories (although these may be governed more by Sharia)—follow the legal concept of succession rules or forced heirship. Property owners are not completely free to distribute estates as they wish. There are rules against disinheriting certain kin—primarily the spouse, children, and grandchildren—and also potentially grandparents and other family members. The rules typically apply to the estate as a whole, but it is possible that some assets may be excluded and distributed according to the desire of the decedent. Before going on, it is important to note that in most situations, laws in the decedent's domicile (i.e., where he or she was living) at death take precedence for estate distribution purposes.

We can use the legal environment of Spain to illustrate[8]. Spain has a system of forced heirship. In that territory, this means that, typically, children are entitled to receive two-thirds of the deceased parent's estate, with some discretion as to allocation with one-third of the assets. The surviving spouse is not entitled to the entire estate. At best, only the remaining one-third may pass to the spouse. This is not atypical for many forced heirship regimes. Some territories following forced heirship rules allow a portion of the estate to pass to the surviving spouse rather than strictly following requirements that might otherwise mandate a large proportion of the assets to pass to children. Also, most territories allow for some portion of the estate to be distributed according to terms of a will rather than forced heirship (e.g., in France, estates are divided into a reserve [forced] and a disposable [elective] portion). It also may be possible to circumvent some or all of the relevant provisions through use of trusts (where recognized) or establishing a foreign corporation to own the property. In some territories spouses can hold property jointly and elect to have it considered as community property. This would allow the property to pass to the surviving spouse. Rules may apply to all property, and especially to real

[8] http://www.solicitorsinspain.com/articles/inheritance-and-forced-heirship-spain

estate in a particular territory. One requirement that many foreign property owners may not be aware of is that even if they live in a territory that does not recognize forced heirship, real estate in a territory that does follow it normally will take precedence. This means if a person lives in England (i.e., testamentary freedom; no forced heirship) and has a house in France (forced heirship), the house will be required to pass according to French estate distribution laws.

A new European Union regulation on succession, known colloquially as Brussels IV, became applicable throughout the EU (except Denmark, Ireland, and the UK) 17 August 2015[9]. The regulation, among other things, allows individuals who have cross-border estates to determine whether laws of their last domicile (where they were living at death) or those of their nationality will apply to their succession. It remains possible in some situations for estate settlement to be referred to the courts to have the applicable jurisdiction's laws determined. However, though the ruling is new, somewhat untested, and not a panacea, it should serve to provide those with a European connection a little flexibility in controlling multiterritory estate distribution.

There are many variations of how forced heirship rules are applied in different territories. Also, although most common in territories following civil law, not all such territories apply forced heirship rules (e.g., China, Mexico). Further, some territories following common law (e.g., Cyprus, India, Jersey, Guernsey) apply at least some portion of forced heirship rules[10]. As always, it's important to know the rules of the specific territories with which you are concerned.

Incapacity

Incapacity refers to the situation where an individual is unable to function normally for his or her own benefit or well-being. The person has inadequate strength or ability to function; that is, has a lack of capacity. Incapacity may apply to individuals at any time, and for purposes of this discussion, refers to a legal disqualification. More specifically, the individual is determined, primarily for medical, emotional, or psychological reasons, to be incapable of entering into, or carrying out certain types of, agreements or activities. As an example, consider an individual who is in a medical coma or who suffers from cognitive impairment (e.g., dementia). He or she is not able to make decisions for their own benefit. Unfortunately, unless the individual has made prior arrangements, once incapacitated, they cannot express their desires regarding things such as ongoing treatment, life-extending measures, and the like. We will look more fully at incapacity in a later chapter and consider planning methods in preparation for the possibility of becoming incapacitated.

Taxable, Probate, and Gross Estate

There are three terms you may see in reference to a person's estate: taxable, gross, and probate. Depending on the territory, the transfer of a person's assets to heirs may be wholly taxable, partially taxable, or not taxable at all. As a result of the potential taxability, we need to recognize the difference between a person's *gross estate* and his or her *taxable estate*. In simple terms, the gross estate is everything a person owns, while the taxable estate is any amount subject to taxation on transfer or distribution (which may or may not include everything)[11]. Depending on the territory, this description can become more complicated, but it will work for our purposes. *Probate estate* includes assets that pass according to a person's will or via rules of intestacy. In other words, it must go through the probate process. The three

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[9] http://ec.europa.eu/justice/civil/family-matters/successions/index_en.htm (Regulation 650/2012)

[10] https://www.cfainstitute.org/programs/cfaprogram/courseofstudy/Documents/estate_planning_appendices.pdf

[11] Gross estate and taxable estate may be identified differently in various territories. The concepts should be generally applicable—gross estate referring to the sum total of a person's possessions, including debts, and taxable estate being any amounts on which a tax/duty will be levied.

terms—taxable, gross and probate—do not necessarily refer to the same group of assets. That is, some of the gross estate may have to pass through probate, but some likely will not. Some of the estate (gross or probate) may be taxable, but some may not. Clients will be concerned about how their gross estate is distributed. They also likely will want to limit applicable taxes and may want to reduce the assets that pass through the probate process. They want this done efficiently and effectively. The primary goal is to manage the distribution in a way that fulfills the client's goals and desires. As a result, financial planners should concentrate on learning what the client wants to have happen, and then look at ways to make it happen efficiently with minimal expenses.

Gifts

Not all estate planning happens postmortem. It may be advantageous and desirable to distribute property prior to death. This is the process known as gifting and it forms a key part of many estate plans. Simply said, a gift is made when the donor during his or her lifetime transfers ownership of property to another individual or entity. Technically, a gift must be complete to qualify as a gift. *Complete* means the property owner has relinquished all control over the property being transferred. This is not necessarily as straightforward as it might seem. Some individuals may transfer beneficial use of an asset, but not true ownership. For example, an individual may place an income-producing asset in a trust or other vehicle and direct the income to be paid to some other individual or entity for a period of time, after which the asset reverts to the original owner. Even though the donor is providing for income to flow to the recipient, this is not a completed gift. The original owner has not relinquished control over the asset. He or she directed what is to happen to the income and reserved the right to retake the asset at some point in the future. The scenario could be reversed with similar results. The grantor may gift property and designate that he or she will receive income for a period of time, after which the property will be owned by the individual/entity who received it (i.e., grantee). It will not be a completed gift until ownership, with no strings attached, is vested in the grantee.

Why make a gift at all? There are many reasons, one of which is to provide some current benefit to a family member, another individual, or organization. If an individual gives something to a child, he or she gets to see that child enjoying the gift. For many people this is reason enough to give. Another reason to give a gift is to reduce the eventual size of a person's estate by the value of that gift. For example, if a client gives a family member a gift valued at $500,000, the donor's estate value will be reduced by $500,000. It is likely that if the estate is subject to taxation, taxes will be less as a result of giving the gift and reducing the gross (and taxable) estate. Further, future growth of the asset will have been removed from the grantor's estate. However, some territories tax gifts, especially those of significant monetary value.

Territories have different rules defining and affecting lifetime gifts. Clients must follow the rules if their desire is to reduce the potentially taxable estate. It is not uncommon for an asset that someone thought was a gift (for estate planning purposes) to be disallowed because of a technicality. Further, some territories have a lookback period that may cause a gift to be brought back into a person's estate. As an example, in the UK, if a donor made a lifetime nonexempt gift of £200,000 five years ago and died today, Her Majesty's Revenue and Customs (HMRC) would likely recall the value of the gift and add it to the decedent's estate, because the death was within seven years of making a nonexempt gift. Depending on specific circumstances and the manner in which the gift was made, the lookback period could be increased to 14 years[12]. The

[12] https://www.thegazette.co.uk/all-notices/content/100654

gift amount would then be subject to inheritance tax (IHT), which is not what the donor desired. We will explore gifting in more detail in a later chapter.

We have said that one aspect of estate planning is tax reduction, but that is not the only, or perhaps even primary, goal. We will look into estate planning and wealth distribution goals in the next chapter.

Discussion Questions

1. Overall, how do common and civil law territories differ regarding succession practices and estate planning?
2. Is the probate process generally positive, negative, or a combination of the two?
3. How is a living will different from a testamentary will (i.e., last will and testament)?
4. What are some of the different property ownership (titling) arrangements and how may they impact estate distribution?
5. How may a forced heirship regime impact a decedent's estate plan?

1. Chapter ReviewWhat is an estate?
2. What are three types of property and ownership arrangements?
3. What is an inheritance and what ownership rights does it involve?
4. How do present interest and future interest differ?
5. What is common law and where is it applied?
6. What is civil law and where is it applied?
7. What is probate and what property generally does or does not pass through it?
8. What is the purpose of a testamentary will and how may it be used?
9. When would a person use a living will or advance directive?
10. What are will substitutes and how do they impact potential probate estate property?
11. What is the simplest form of property ownership?
12. What are the types of joint property ownership?
13. What is the primary identifying factor for community property?
14. What is the main characteristic of a forced heirship scheme?
15. What makes a gift "complete"?
16. Would a donor who places an income-producing asset in a trust and directs income to be paid to another individual or entity be credited with making a completed gift?

Chapter 2: Estate Planning and Wealth Distribution Goals

Learning Outcomes

Upon completion of this chapter, the student will be able to:

2-1 Distinguish between estate planning goals
2-2 Determine constraints to meeting estate planning goals

Introduction

We introduced the course with a quote from Roy Diliberto:

> *Imagine asking someone on his death bed how he would like to be remembered and getting the response: "As a person who had an estate plan that saved taxes" (Diliberto, 2006, p. p 105).*

Diliberto's quote makes a good point. Clients almost always are interested in saving money on taxes, and that should be recognized as one of the goals when you develop a client's estate plan. However, as Diliberto suggests, reducing taxes is not likely to be a client's primary estate planning goal.

At its heart, an estate plan is a strategy that allows an individual, when he or she dies, to distribute assets to the people and/organizations they choose, in the manner they want (Barrow, 2017, p. loc 187). The *manner they want* typically includes efficiency and with as little reduction of the estate as possible so that heirs receive the largest potential inheritance (that's where keeping taxation minimized comes into play). Saving taxes is not the primary goal; it is a tool supporting the primary goal, which is to distribute assets to heirs efficiently and effectively.

Discovering Client Goals

If you were to look at a client and say something like, "Tell me your estate planning goals," you may be faced with a shoulder shrug and a blank stare. The client probably has some ideas, but does not know how to articulate them. It's up to you as the financial planner to engage the client and discover not just their goals, but also the motivations behind them. In other words, as is true with all of financial planning, a good financial planner will invest the time to get to know the client and to understand not just what they say they want, but also why. If this discovery process is a primary planning goal, how do you go about doing it?

A key component of a beneficial discovery process is for the financial planner to be curious about his or her client. What are their motivations? Why do they want this or that? Are there underlying factors that seem to be moving them in one direction or another? What do they *say* they want and what do they *really* want—is there a difference between the two? Sometimes, an estate planning discussion seems to be going nowhere, and the planner can tell that one or more factors are influencing the client, but the client isn't letting the planner know what they are. Marcee Yager, a financial planner who does estate planning, recounts a story that can shed light on why this may be so (Diliberto, 2006, pp. 109, 110):

> *In this case, her clients, Joan and Dick, were recently married—both for the second time with children from their previous marriages. Joan had inherited a family trust and was wealthy, but Dick had little left from his divorce settlement. He earned his money by buying real estate, remodeling it, and selling it. When Marcee first asked him what he wanted, he told her that he wanted everything he owned to be in community property because he believed in the marriage partnership. So Marcee told him how that would work. Then he said, "Okay, but now my kids will get nothing." She suggested that he purchase life insurance for their benefit. He thought that was a good idea, until he objected to paying premiums just to ensure that his children would get money. She couldn't get him to articulate what the real issue was. On the one hand, he wanted everything in community property. On the other hand, he felt poor, because "what's his is hers and what's hers is hers." No matter how many plans were devised, he refused to sign off on any of them. It was becoming apparent to Marcee that something that he wasn't sharing was bothering him . . . .*

What do you think Marcee did? What would you do in a similar situation? Would you be able to move forward, or would you just let things go and write it up as a failed engagement? Let's see what Marcee did.

> *Marcee stopped suggesting solutions and began to concentrate on his [Dick's] issues. She said, "I need your help. You are torn between two conflicting goals, and I need clarity about what is troubling you so I can make this work for you." After several meetings and much discussion, he told Marcee, "I feel so guilty for having gotten a divorce and so angry about the effects of that. Having to give my ex-wife so much of what I owned and being estranged from my kids has caused me to be anxious about money. My new wife is rich and can support me, but I am an old-fashioned guy and I'm torn up over this." It was clear to Marcee that they needed an estate plan that would consider these feelings, and that taxes had no bearing on these feelings.*

While Marcee could have given up, instead, she did what a financial planning professional ought to do. She asked her client to share with her the nature of his concerns. It required some time, but ultimately, Marcee, with full agreement from Dick and Joan, was able to craft an estate plan that appealed to both clients and accomplished their goals. She would not have been able to do so if she didn't refocus and begin asking questions to clarify her understanding.

Clients doing end-of-life planning (e.g., estate planning) generally have a primary interest in leaving a legacy. Here are three questions you can suggest they ask themselves to facilitate the discussion (Diliberto, 2006, p. 111):

1. What was the meaning of my life?
2. Did I make a difference in the world?
3. What is my legacy to the world?

These questions, and similar, can help the financial planner guide clients to ensure their estate plan and the legacy they leave reflect their core values.

Common Estate Planning Goals

Let's identify some common estate planning objectives of married couples. Most of the objectives also apply to the unmarried, adults with partners (rather than spouses) as well as others. Some estate planning objectives/goals include (Saret, 2014):

- Provide for loved ones. Financial security is one of the most important goals for most couples wanting to ensure that their loved ones are provided for when one of them dies or becomes incapacitated.
- Minimize taxes—. It may not be the primary goal, but it’s certainly a common goal, so that more assets pass to heirs rather than the government if at all possible.
- Protect assets passing to surviving spouses/heirs—. Minimizing threats is mostly about keeping assets protected from creditors and any who would try to take over assets unscrupulously.
- Make it simple and inexpensive—. Make estate plans easy to follow for heirs (including the surviving spouse/partner) without undue costs, but not at the expense of accomplishing overall objectives.
- Keep things private—. Maintain privacy to the degree possible.
- Have control over assets—. Maintain control over assets to the maximum extent possible.
- Plan for potential incapacity—Make arrangements to address myriad potential needs in the event one of the individuals becomes incapacitated in some way.
- Manage assets—Put into place systems to assure positive financial management when one or both is no longer capable of managing family assets.

We can add a few items to the list, such as avoiding disputes among family members, business partners, or related third parties; provide for one or more charities; provide adequate liquidity to settle the estate; or transfer any business ownership to heirs.
Additionally, two good questions to ask, more in line with the technical side of things are[13]:

- Do any of the heirs/beneficiaries need protection, and if so, from whom?
  This could be a situation where an elderly person is mentally incompetent, or nearly so; a minor who is likely to overspend inherited assets; creditors; even siblings and former spouses.
- Who will act for the individual when he or she no longer is able to do so?
  It should be clear that you, as the financial planning professional, will not be able to answer these questions. However, you can ask them and guide the clients to consider and develop answers.

Notice how few of the goals focus on reducing transfer taxes or other expenses. Those goals are there, to be sure, but other aspects seem to take precedence. Three areas of significant importance relate to loved ones (family), children (and grandchildren), and philanthropy.

Providing for Loved Ones

This is perhaps the most commonly expressed estate planning goal. A consistent theme is to provide financial security for loved ones and to ensure they are provided for when the estate owner dies or becomes incapacitated. Passing on assets is one aspect of doing this. Parents often want to ensure their children inherit important family assets to continue the family legacy throughout posterity. Even more immediately important and practical is the desire to provide the family with enough money to continue living in a desired lifestyle. In this regard, illiquid and perhaps unmarketable assets are far less useful than cash and overall liquidity. Providing adequate liquidity effectively can be more difficult in some territories than in others, especially in forced heirship regimes. Life insurance is sometimes used for this purpose.

[13] https://www.wellsfargo.com/the-private-bank/insights/goal-based-planning/

Specifically, when a spouse wants to ensure the surviving spouse has adequate liquidity and cash flow, a valid will, and perhaps a trust (where applicable), life insurance or an alternative is likely to be required. Part of the reason for this is that, especially in territories with mandatory succession rules, the surviving spouse may be required to share estate funds with the children. While this may sound equitable, often it is not. Consider the following situation:

> **Example.** The decedent has an estate valued at $1 million and is survived by a wife and six children. Further, the wife is not able to work and generate income. The decedent might reasonably want the wife to receive all of the estate, knowing she will continue caring for the children. However, when mandated by succession laws, the estate may be divided seven ways. In such a situation, the wife would only receive $143,000 and each child would receive the same amount. This may seem fair on the surface, but reality likely will be different. From her share of the estate, the wife will be required to support herself along with the six children. The children, however, will not be required to use any portion of their inheritance to support themselves. As a result, the wife's $143,000 will quickly be used up, while each child's inheritance will remain untouched. This will leave the wife in a difficult place, and potentially not able to care for the children. She may even have to move out of the family home due to lack of funds.

Recognizing possible difficulties, many territories' rules allow the surviving spouse to receive a larger portion of the estate. In turn, surviving spouses will be better able to support themselves along with the children. This does happen, and it is a good reason to clearly state distribution goals in a will. Identifying distribution goals does not always solve the problem, but often it does, and a well-constructed will, along with funding vehicles already mentioned, almost always improve the likelihood of the decedent's wishes being enacted.

Potential or existing incapacity is another area of concern. We will cover incapacity in a later chapter, with a focus on a client's possible future incapacity. It may be, however, that one or more of the survivors currently is incapacitated in some way. Maybe the spouse is unable to care for him or herself. One or more children may require special, ongoing care. Perhaps one or more parents may need extended care at home or in a dedicated facility. Each of these situations will require attention when making plans. Physical or mental incapacity can be difficult for family members to address. It also can be financially difficult to manage the ongoing care for the incapacitated individual(s). While most families accept this as part of family responsibility, the fact remains, funds must be provided, and arrangements made to continue caring for incapacitated dependents.

Children and Grandchildren

Providing for children is a common estate planning goal. In addition to providing funds while children remain dependent at home, a good estate plan will include provision for assets children will be able to use as they reach majority. This goal probably will require naming an administrator or trustee to oversee disposition of inherited assets. If the estate is small, not much will need to be done. However, if the estate is large, administration may require thorough planning and clear instruction to provide direction for administrators (trustees, guardians, solicitors, etc.) on how to distribute assets over time.

An individual may have many goals for children. Here, we will highlight two of those that are possible. The first applies to all children, but especially to those in families of typical or modest financial means. What do all parents want for their children? Simply said, parents want to ensure their children/grandchildren (especially minors) are cared for and supported; that they have every opportunity to grow into adulthood safely and well-positioned to succeed in life. When the parents are living and the family is whole, they will work together to accomplish this goal. However, when one or both parents dies, and they no longer can directly care for their children, they usually will want to arrange for their children's well-being in their absence.

A big part of providing for minor children is to have adequate funds available for food, clothing, general care, and related expenses. Parents also may want to provide for their children's higher education. We can identify three common needs: First, sufficient funds to provide for living expenses. Second, because minor children cannot (and usually will not be allowed to) manage money for themselves, a guardian or administrator to oversee the funds. Third, someone to care for and guide the children as they grow to majority and independence. This may be a family member, a trusted friend or neighbor, or perhaps even an agency. Regardless of who steps into the position, the children will need guidance from someone, and this is something parents should consider and arrange prior to death. Obviously, they cannot keep their decision a secret, and will have to gain agreement from those chosen to embrace the new responsibilities. Parents who do not make these arrangements run the risk of having the state/courts determine who will care for the children. This is seldom consistent with parental wishes, so it becomes an area to be addressed early—shortly following birth is not too soon.

Children are usually not considered competent to manage money on their own. They simply do not have the knowledge, skills, or abilities to do so. As a result, most jurisdictions require a guardian or administrator to be appointed who can oversee funds for the benefit of the children. Usually, this is done under state supervision and requires regular reporting to the state or a designated agency. Where they are recognized, some parents may wish to establish a trust that will hold assets for the children. Trust terms normally include how income and assets may be distributed to the beneficiaries, and under what circumstances. Often, there may be instructions to allow whatever funding is needed to provide for the welfare of the children. The trustee(s) will be instructed to do this, along with any restrictions the parents impose. The trust agreement almost always will provide instructions for how any remaining assets should be distributed once the children reach the age of majority (or at some later age).

Education funding may or may not be needed, but when it is, it may come under a separate arrangement. Some parents will prefund any tuition or other higher education expenses. Others may direct life insurance proceeds to be used for that purpose. Funding may be placed in a trust, may be paid directly to the educational institution, or may be made available to the administrator for the stated purpose. Life insurance proceeds often are used to fund this goal, providing an efficient, cost-effective way to do so. Care should be applied when determining appropriate beneficiary arrangements. These may include payment directly to a trust or other institution for the express benefit of the children. As with other financial amounts, causing funds to be paid directly to children seldom is wise, and may not be legal.

All of the preceding observations are applicable to grandchildren as well as children when this is desirable.

Children of High Net Worth Individuals (HNWI)

Parents who are HNWI may have additional concerns when planning for their children. Specifically, legacy planning for these individuals can become a more complex undertaking. As is true of most children, heirs of HNWI often are not prepared to handle large sums of money. Additionally, depending on the family, there may be issues related to how the surviving family relates to society, staff, various organizations (including philanthropic), and others. Often, very HNWI live under increased scrutiny, and this may be a burden on their children. Sometimes, HNWI have not adequately prepared their children to become responsible heirs, and this can create an added layer of difficulty.

To a large extent, children are children, whether they are raised in an HNW home or one with less financial well-being. For our purposes, we want to address how to help children—specifically those in HNW households—cope with large amounts of money. The time to start this process is early in the child's life. HNW parents, as is true of all parents, must help their children learn the value of money, which includes what money is not and cannot do. There are several money myths that children may believe. Among these are (Mellon & Christie, 2014, p. 43):

Figure 1: Money Myths of Children

Money	=	Happiness	Money	=	Freedom
Money	=	Love	Money	=	Self-worth
Money	=	Power	Money	=	Security

Many people in the world believe one or more of these myths. The truth is that money does not equal any of these things. Money is a tool. It can be used for good or ill, and it does not, by itself, produce happiness, love, power, freedom, self-worth, security, or anything else. It can be helpful in achieving these things, but it must be effectively and efficiently applied to do so. People without money continue to be able to achieve each of these outcomes. One of the difficulties for children in HNW homes is they may have more incentive to believe these myths. Parents must therefore step in to help children learn core truths about money. This is most difficult when one or both parents believe the myths. As a result, the children likely will head down the same road as their parents. The preceding relates strongly to the topic of leaving a significant financial legacy to children. Unless they are taught early how to properly address and use money, children will be ill-prepared to receive their inheritance.

It seems one of the primary problems of *affluenza,* as it has been called, is a false sense of entitlement (Furnham, 2014).

29 Dec 2015, BBC UK. Ethan Couch, 18, and his mother Tonya were taken into custody in the west coast resort town of Puerto Vallarta (Mexico). An arrest warrant was issued earlier this month for Couch after he failed to report to his probation officer.

Couch became known for his unusual defense, which argued his privileged upbringing was to blame for the crash. On June 2013, at age 16, Couch was driving drunk and speeding on a dark road when he crashed into a stationary car, killing four people and injuring several others, including passengers in his own pickup truck.

During the sentencing phase of his trial, Couch's attorneys argued that the teenager's wealthy parents failed to instill a sense of responsibility in him—a condition the expert termed "affluenza." He pleaded guilty to four counts of intoxication and manslaughter, and two counts of intoxication assault causing serious bodily injury.
http://www.bbc.com/news/world-us-canada-35192267

To help overcome this, over the years, many HNW parents have attempted to instill core money values in their children. One such value is learning to give to others. As an example, parents may help children donate clothing; assemble and deliver food baskets; help neighbors—especially those elderly or disabled, with projects around the house, such as raking leaves, going grocery shopping, or picking up trash; or dedicating part of an allowance to a charitable cause chosen by the children[14]. Parents can join their children in doing service projects. Some parents have taken children on one or more trips to impoverished places with the goal of helping people there by serving them in some way(s). Parents can include children in some of the decisions they make regarding to whom and in what ways the family can reach out and share with others. This does not have to be monetary in nature to accomplish the purpose, although teaching children how to share money also is beneficial. Parents may even want to help children set aside a portion of their own money to contribute to a donor-advised fund or similar philanthropic vehicle[15].

Why all this about philanthropy? It's about attitude. When children (especially from wealthy families) learn early in their lives that having money is not a *right* and something to which they should feel entitled, they gain some perspective on having money. Perspective will help when they receive a substantial inheritance. When that happens, they already will have *right-thinking* about money in place. This will help them keep things in perspective.

Of course, parents should ensure their children learn how money works and how to work with it. Enlisting the help of a qualified mentor or advisor (such as a financial planning professional) can be beneficial in this respect. It's not uncommon to see stories of suddenly rich young people indulging themselves, taking advantage of others, and generally getting themselves into trouble. HNW parents will be well-served to keep all this in mind and prepare their children early and well to embrace right-thinking and right-acting about money.

As a practical matter, parents also should consider establishing a trust, guardian, administrator, etc., to place some parameters around children's use of an inheritance, especially when they are first learning how to cope with the sudden money.

Providing for Organizations and Others

Leaving a legacy is a common theme among HNWI and others who want the wealth they have to be distributed in a manner that allows them to make a difference in the world and leave a legacy that is meaningful to them. There is an old proverb (likely originating in England) that says, *Charity begins at home*. While some may question the veracity of this saying, there is no question that, for most individuals, the desire to take care of loved ones takes top priority. That said, for many people with the financial means to do so, supporting a cause or organization they believe in has great significance as they think through their estate planning.

The rules for distributing wealth to various causes and the organizations that support them vary by territory as well as by the nature of the organization. If the organization is recognized as being legitimate or is otherwise approved by the government, wealth transfers may be more easily accomplished than if the organization does not have that status. Some territories allow for both testamentary or *inter vivos* charitable gifts to be fully or partially tax-free, while others do not. Even where there is no taxation, the amount that can pass tax-free may be limited. Territories with strict succession laws can make giving to nonfamily beneficiaries difficult to the point of being nearly impossible. Where they are allowed, one or more trusts can be used as a vehicle to hold assets/money to be given to a charitable organization. Some universities have endowment-type plans to facilitate gifts from alumni and others. Usually small gifts are absorbed into the university's general finances, while large gifts may be designated to provide

[14] https://www.parents.com/parenting/money/donate-to-charity/9-ways-to-teach-your-child-about-charity/

[15] https://www.nptrust.org/what-is-a-donor-advised-fund

scholarships, fund faculty salaries, support research, even build libraries or other buildings. Regardless of the organization and the size of the gift, philanthropy often is an estate planning goal.

Small Business Owners

Some clients will fit into the category of being owners of a small business. In addition to estate and wealth distribution planning concerns common to many clients, small business owners may have anxieties related to their business—keeping it going, allowing the family to gain a benefit from it, and distributing ownership in a way that helps accomplish the first two concerns. Often, a business owner has invested a majority of time, effort, and finances in the development of the business. Most owners receive current financial benefit from the business. They also count on the business to provide for them at retirement. Further, partly as a result of having invested so much of their resources in the business, owners normally intend for disposition of the business at their death to provide for their family. This typically requires determining the way in which the business can be transitioned from the original owner to a family member, or perhaps to a third party.

According to a study of small family business owners in the UK, here are a few of the top estate and distribution-related concerns (Family Business United , 2017):

- Continuing to develop and remain a profitable business
- Management succession planning
- Planning for later life
- Engaging and developing the next generation
- Ownership succession and developing responsible future owners
- Identifying and maintaining family values
- Extracting value from the business
- Taxation

Notice how many of their concerns focus on being able to transfer a thriving business to younger family members or another owner who will help accomplish their goals. A few additional areas identified ongoing business development interests, but the majority of the list shows how interested the small business owners in the survey group are regarding business succession.

Accomplishing these objectives begins by developing a plan. Also, it's best to start planning early—probably earlier than the business owner may think necessary. Here are some points to consider in a succession plan (SBDC, 2016):

- The successor; family member, business partner, other
- Succession type; partial or full succession
- Timeframe
- Key personnel changes and skill retention strategies
- Restrictions
- Legal consideration; buy-sell agreement, reference to a will
- Risk management
- Communication strategy
- Financial considerations; retirement income, sale prices, tax implications

You may or may not be familiar with buy-sell agreements[16], but they can be helpful when working to transfer business ownership. As with most legal documents, there may be a bit of

[16] A buy-sell agreement is a legal document that must be drafted by a competent, licensed attorney

variety in composition as well as application, but we can highlight a few consistent elements (SBDC, 2016):

- Who can buy the departing owner's share of the business
- The circumstances that allow the share of the business to be sold, such as retirement, death, disability, or leaving the business
- The price that will be paid for the share of the business

A few of the considerations highlight transitions prior to death, but most apply to business distribution related to the death of the owner. One of the considerations may be to try selling the business prior to the owner's death. If the business cannot be sold, the family should have plans to suspend business operations or perhaps hire someone (or a firm) to manage the business. This can be a valuable solution when the current environment is not especially conducive to selling the business, but where that situation is anticipated to improve in the near future. It's almost always easier (and more profitable) to sell a business that is successfully being run rather than one that is failing.

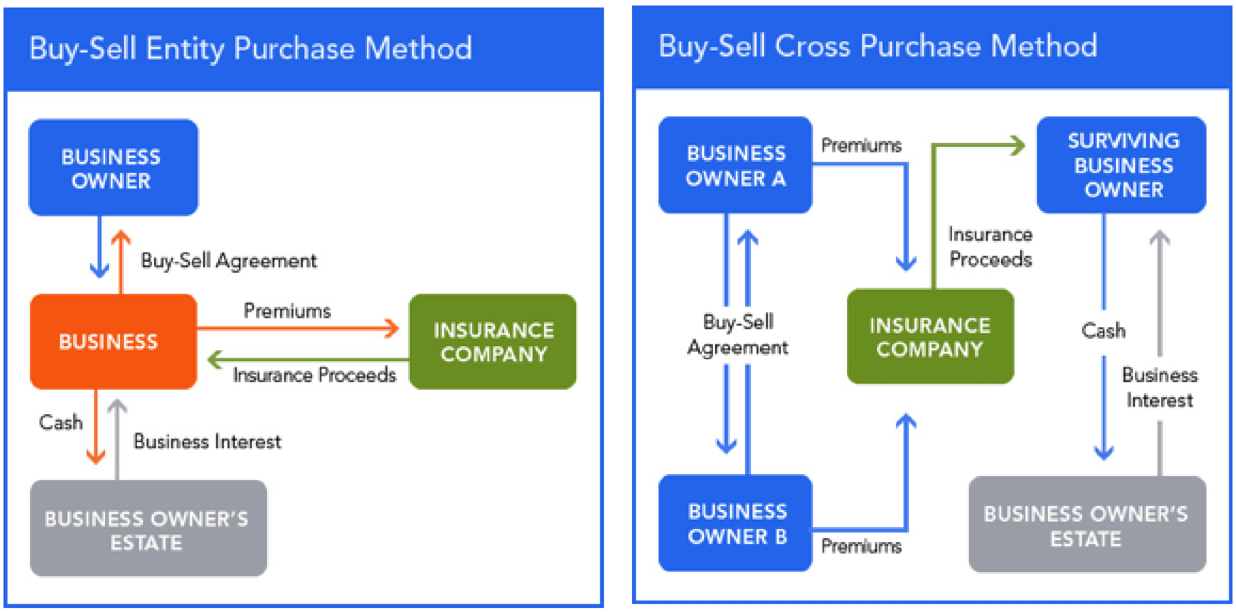
When a small business has more than one owner (whether a corporation or partnership), the remaining owners may wish to purchase the decedent's share. This is one of the considerations to include when drafting a buy-sell agreement. Normally, if the business is organized as a corporation, the business itself may purchase the outstanding shares. With a partnership, generally, each remaining owner will agree to purchase the decedent's ownership share.

Regardless of business organization structure, there will be a few common objectives. The first is to keep the business going. Depending on the business size, it's likely to have employees who would like to continue working. Also, the remaining owners, if any, almost certainly wish to continue earning an income from the business, as well as having the value of their ownership share increase. The family of the decedent also will have related concerns, chief of which is how they can recover the decedent's investment. Also, it's likely they were counting on an ongoing income stream from the business, and now they will be concerned that the income will cease. A well-constructed buy-sell agreement will address each of these concerns.

Funding is one item that will be necessary. Whether the corporation purchases the decedent's shares or the remaining partners do so, they will require money to purchase the business interest from the decedent's spouse and/or family. Typically, when a business owner dies, his or her share of the business will pass on to the surviving spouse or other family members. This is good because they now have ownership of an important asset, but often, that has little practical value. Most times the spouse or family is not competent to manage the business, or they do not desire to do so. What they want is financial remuneration. This supports the desires of the remaining business owners, because they most likely would prefer the surviving family to stay out of the business. At the same time, they recognize the need (and probably are mandated by terms of the buy-sell and/or other agreements) to settle with the decedent's spouse and family. The simple solution to this is for funds to be available for the remaining business owners to purchase the decedent's share from his or her spouse and family. That solves the ongoing ownership concerns and provides the family with the money they desire to support their lives.

There are several ways to provide the funding, but one of the more common methods is through use of one or more life insurance policies. The business may own a policy on the owners (e.g., entity agreement) or each of the owners may own a policy on each of the other owners (e.g., cross-purchase agreement, also known as a cross-option agreement). Regardless of the manner of life insurance policy ownership, the end result is the same: The money is made available for the remaining owners/corporation to purchase the decedent's business share from the surviving spouse/family. In doing so, each party's interests are supported. In lieu of life insurance, the business may establish a sinking fund to make the eventual purchase. Another alternative is to make installment payments from the business to the surviving spouse/family. Doing this delays receipt of some income, but with a properly executed agreement, guarantees financial provision for the spouse/family. There are other options, which may include borrowing money or seeking a third-party buyer, but ultimately, the goal remains the same. Only the funding and purchase agreement varies.

Figure 2: Entity and Cross-Purchase Buy-Sell Agreement Example (Western & Southern Life, 2017)



Now that we have explored some common goals, we have to consider the question, "What process should clients follow to carry out their estate planning and wealth distribution wishes?" This is the subject of the next chapter.

Example 1		
Question		*Typically, when a business owner dies, his or her share of the business will pass on to the surviving spouse or other family members. This is good because they now have ownership of an important asset, but often, that has little practical value. Most times the spouse or family is not competent to manage the business, or they do not desire to do so. What they want is financial remuneration. There are several ways to provide the funding, but one of the more common methods is through use of one or more life insurance policies. Which of the following statements is most likely correct?*
	A.	In a buy-sell cross purchase method, the business pays the insurance premiums.
	B.	In a buy-sell entity purchase method, the buy-sell agreement is between Business owner A and business owner B.

	C.	In a buy-sell entity purchase method, the business pays the insurance premiums.
	D.	In a buy-sell cross purchase method, the business receives the insurance proceeds.
Correct Answer		**C.**
Explanation		In a buy-sell entity purchase method, the business pays the insurance premiums is true.
Distractor #1	**A.**	In a buy-sell cross purchase method, business owner A pays the insurance premiums. The surviving business owner then uses the cash to but the business interest from business owner's estate.
Distractor #2	**B.**	In a buy-sell cross purchase method, the buy-sell agreement is between Business owner A and business owner B.
Distractor #3	**D.**	In a buy-sell cross purchase method, the surviving business owner receives the insurance proceeds.

Discussion Questions

1. How would you conduct a discovery session so you can understand a client's estate planning goals and hidden concerns?
2. How can HNW parents prepare children for an eventual (large) inheritance? How might this be different than with non-HNWIs?
3. What steps can be taken to help children break through any money myths to which they might hold?
4. When developing an estate plan, how might a small business owner and family handle business distribution concerns?

Chapter Review

1. What three questions can clients ask themselves to facilitate an end-of-life discussion?
2. What are some common estate planning objectives, especially for married couples?
3. What two questions can a financial planner ask to address potential concerns related to heirs who may not be in a position to take care of themselves?
4. In addition to distributing assets to family members, what is a common desire and need for a decedent to take care of family?

1. Why may forced heirship be a potential problem for surviving spouses?
2. What are three common needs parents may have for dependent children?
3. What action will most jurisdictions take to protect children's financial assets from their inheritance?
4. What are six money myths children may believe that can harm them?
5. One identified potential problem when HNWI's children inherit a large amount of property is called affluenza. What is affluenza and how can it be addressed?
6. As a practical matter, what may parents do to help heirs handle their inheritance?
7. What are some of the top estate-related concerns of small business owners?
8. When developing a business succession plan, what points should be considered?
9. There are three consistent elements in most buy-sell agreements. What are they?
10. When the current environment is not especially conducive to selling the business, but that situation is anticipated to improve in the near future, what can surviving family members do to continue business operations for a period of time?
11. What are some common business objectives following the death of an owner?
12. What is a common method to provide funding related to a buy-sell agreement?

Chapter 3: Estate Planning Process

Learning Outcomes

Upon completion of this chapter, the student will be able to:

3-1 Develop steps in the estate planning process
3-2 Determine estate value at death
3-3 Evaluate ways to reduce taxes and expenses at death

Introduction

The estate planning process will vary significantly from one territory to another. At the most basic level, some territories exert control over how an estate is distributed—through taxation, succession laws and other mandates—others have a more *hands-off* approach, essentially allowing estate owners to distribute property in whatever way they choose. Most territories fit into the gap between the two extremes. Some degree of taxation is common, even when a territory does not specifically levy a tax on all property transfers (during life or at death). Similarly, most territories have rules regarding intestacy and/or mandatory succession statutes. This chapter will focus on the monetary aspects of estate planning: determining net worth, calculating potential expenses and taxes, and ways to reduce taxes and expenses and provide liquidity. We will begin looking at steps in the estate planning process.

Steps in the Estate Planning Process

Every person has a unique situation. This is as true of estate planning as it is more generally of financial planning. This means you cannot simply follow a set pattern of steps that is the same with every client. However, we can identify steps that should be part of most estate plans (Northwestern Mutual, 2014):

- Create an inventory of what is owned and what is owed
- Develop a contingency plan
- Provide for children and dependents
- Protect assets
- Document wishes
- Appoint fiduciaries/legal representatives

Let's look at each step more closely.

Create an Inventory

Creating an inventory may or may not be a mandatory legal requirement, but it's always a good idea. This includes things like account numbers, contact information, medical personnel, online login information (i.e., username, password and URL), as well as all physical property (real and personal) investment assets, and anything else of value. This list also should include current debts and related information (amounts owed, to whom, payments, etc.). It's a good idea to include contact information for financial and other advisors. The list, and supporting documents, should be kept in a secure location that can easily be accessed by surviving spouse, heirs, and legal representatives. The client should make a summary of the information and provide it to the people who should have the information. Clients should be careful where they keep the documents. Many banks and other institutions require quite a bit of proof that someone has the right to access the information. This can take a lot of time and unnecessarily delay the process.

Develop a Contingency Plan

The overall estate plan identifies a client's wishes for distribution of property and assets and provides guidance for ongoing care of children and dependents . . . if everything goes as planned. Sometimes, rather than reach the end of life, an individual may become incapacitated. When this happens, plans already made may have to be amended. For example, how will expenses be paid and how will dependents be provided for? In addition to addressing these things in an estate plan, it is a good idea to create a contingency plan in the event of incapacity or some other unplanned event.

Provide for Children and Dependents

This is a primary goal for most people. Parents want to protect and provide for surviving children and dependents (i.e., parents, siblings, etc.); one spouse wants to provide for the other. There is, of course, a financial aspect to this that provides short-term liquidity (cash flow) and provision for ongoing expenses and plans. Perhaps a fund to help a child get started in business, purchase a home or pay university expenses will be desired. A husband or wife may want to ensure their spouse has enough to sustain them for a period of years or for life.

Minor children will require a guardian and an administrator until they reach the age of majority or perhaps some later age. There may be children from a prior marriage to consider. Also, children and dependents with special needs will require additional planning for care and funding.

Protect Assets

Clients want to ensure their assets are distributed according to their wishes. This means, in part, those assets must be protected so they can be passed on. Protection includes minimizing expenses and keeping taxes to a minimum as much as possible. Protection also includes keeping assets out of the hands of creditors and others who may not have any real claim to them. Clients also will want to ensure that all assets are included in their plan, and that special assets, such as a business or investment property, are transferred appropriately and with minimal expense.

Document Wishes

This step involves more than creating a wish list. Estate distribution plans must be legally documented and appropriately filed. Having a current, valid will is the often first step in this process (we will look at this below). This step also includes nominating/naming beneficiaries for life insurance policies, annuities, retirement accounts (as appropriate), and other financial instruments. Clients often have assets that are titled solely in their name, such as vehicles and real estate (property). They need to clearly identify how they want these assets to be distributed and retitled. A living will, power of attorney for medical treatment, enduring (or springing) power of attorney, or other document stating end-of-life desires and addressing health care concerns should be drafted. If a trust will be used, that will need to be established and documented as well.

Appoint Fiduciaries/Legal Representatives

The client should be reminded that they won't be around to ensure their wishes are followed. Someone will have to be appointed to act on their behalf and carry out their plans. This may include legal representation to settle the estate (i.e., an executor), one or more trustees to manage assets, legal guardians and administrators for children, and perhaps a personal representative or power of attorney if they become incapacitated. If your territory has a fiduciary standard, the representative(s) should be fiduciaries. If not, the representative(s) should be legally authorized to do what you have charged them with doing. As a financial planning professional, you may be asked to be part of the team. If you are able to do so, you will provide a valuable service to your client, as well as their surviving heirs and beneficiaries.

Creating and Reviewing a Will

Dying without a will usually creates problems. Doing this, or having an invalid will, is known as dying *intestate*. Dying intestate opens estate distribution to laws of intestacy that normally will not reflect the desires of the decedent. One of the first goals of estate planning as part of financial planning is to ensure the client has a valid, current will. In almost all cases, drafting a will is the job of a licensed attorney/lawyer. If you attempt to draft a will without being legally authorized to do so, you almost certainly will be violating your code of ethics along with applicable laws in your territory. Doing so usually is a criminal offense. However, as a financial planner, you can provide guidance as to what the will should cover. Basic functions of a will include:

- Specifying how the individual wants the estate to be distributed at death
- Naming an executor (who will help administer the estate in accordance with the will)
- Naming a guardian/administrator for young (minor) children
- Revoking any previous versions of a will

A simple will may say something like, "all property belonging to me at my death to be distributed, after settling all debts and liabilities, as follows," or similar. Unfortunately, this simple language seldom is effective for any except the most basic estates. Further, it does nothing to address special distribution desires, such as regarding unmarried partners, giving specific items to certain children, or others, unequal shares among children or equal shares among children from both a current and former marriage. It also does not address concerns related to specific succession/inheritance mandates in the territory. Further, it does not take advantage of arrangements that may reduce taxation or other expenses, or provisions that may be used to protect both assets and heirs. At this point it will be good to remember that some property passes outside of a will. This includes life insurance policies, retirement plan arrangements (e.g., annuities, and other plans as consistent with practice in the territory), ownership titling (e.g., joint tenants, tenants in the entirety or in common, etc.), and some financial accounts that have named a beneficiary or include specific postmortem provisions (e.g., *tontine*). Similarly, some territories have mandatory rules about how real property is passed. It may not be possible, for example, to pass ownership of a property in one territory to an heir from another territory.

In many territories it is not possible to disinherit a spouse and/or children. When doing this is attempted, territorial law will override a will. Unless there are unique circumstances in the relationship, it's unlikely a person will want to do such a thing, so the law can serve as a safety net. However, regardless of intent, there are some things a will may not accomplish.

Generally speaking, property that passes by a will is known as probate property (or similar), and that which does not pass by a will is known as nonprobate property. Probate property makes up the probate estate, which is all of the individual's property that passes by a will or laws of intestacy. In some ways, nonprobate property is easier, because it does not go through a sometimes lengthy and expensive probate process. However, a will usually allows the testator more control over estate distribution, and also allows the individual to address any property that may have been forgotten, or arrives following death (e.g., an investment dividend, final payments from work, a car or other assets, etc.). The individual can insert a *residuary clause* in the will stating that all that remains following payment of debts, etc., and specific amounts already identified in the will, should pass to a designated person or organization. It's a catch-all statement that keeps anything from falling into a place where the probate court will have to determine the distribution.

The following provides a checklist of some cautions and areas a financial planner should keep in mind when reviewing a client's will (Parish, 2010, p. 48):

- Review of will by an attorney has not occurred in the past 12 months
- Execution requirements have not been satisfied
- Will was drafted too long ago and laws have changed
- Deletion or addition of one or more beneficiaries named in the will is desired
- Change in the amounts bequeathed to one or more beneficiaries is desired
- Change in the type of property bequeathed to one or more beneficiaries is desired
- Change in the amount of the marital property or in the amount of life income to the surviving spouse is desired
- Change in residuary clause (i.e., property distribution not specified in the will) is desired
- Cancellation of debts by a will provision is desired
- Change in marital status of client (testator) or a member of client's family has occurred since the last review
- Change in the health of client or a member of client's family has occurred since the last review
- Birth or adoption of children/grandchildren has occurred since the last review
- Will does not address potential abatement or ademption problems (i.e., specific property is no longer part of the estate, but is identified in the will)
- There has been a significant change in the value of the client's estate since the last review
- One or more assets have appreciated greatly since the last review
- The estate faces a potential liquidity problem
- There has been an acquisition/change in ownership of life insurance, qualified pension plans, or other retirement benefits since the last review
- There has been a significant change in a business situation since the last review
- There have been business liquidity or continuity problems since the last review
- Change of a guardian, executor, or trustee designation is desired
- Addition of a successor guardian, executor, or trustee is desired
- Change in the apportionment of debts or taxes are desired
- There has been a change in the status of a fiduciary since the last review (divorce, deterioration of health, disability, relocation)
- There has been a change in the form of property ownership or a change on one or more deeds of ownership since the last review
- There has been a change in the jurisdiction of residency since the last review

- Additional property has been acquired in a different jurisdiction since the last review
- There have been significant tax law changes since the last review
- The will needs to be reviewed for additional reasons
- The will contains precatory language (i.e., words that express a wish, but are not legally binding) that a court may not enforce

It's important to remember, when working with cross-border and expatriate clients, if they have a will that was drafted in their home territory, it likely will not be completely valid in your territory. This often is the case, especially when succession laws (e.g., forced heirship) are not recognized in the other territory, but are a part of your territory (and vice versa). As a result, one of the first steps when doing cross-border estate planning is for the client to have the will reviewed by a competent legal representative in the current territory of domicile. Commonly, at least some modifications will be required, and it's better to get this done prior to the client's death. For clients with assets in more than one territory, it is advisable to have a will that is valid in each territory. Care should be taken to assure there are no conflicts between the different wills that might delay settlement or cause some part of the desired distribution to not happen as originally planned.

Letting wishes be known is one of the major reasons to draft a will. For example, consider a couple that is cohabiting, but is not married. Most territories' intestacy rules do not recognize that relationship as being valid when it comes to estate distribution. It's possible that even stating in a will that the client wants a percentage of assets to be distributed to the unmarried partner, territorial rules may override that directive. However, it's almost certain that without a will, the partner will not be able to receive any part of the estate. Other desires can similarly be impacted by lack of a will. Just about any distribution plans that fall outside of spouse, children, and other family members will not be followed when a person dies intestate. They will not be able to give assets to charitable organizations, friends, universities, or similar (unless listed as beneficiary of a life insurance policy or other asset that passes via a recognized will substitute). In short, any client who wants to specify all or part of how an estate is settled should have a current, valid will.

Another potential problem of not having a valid will is that some territories will follow a path that is unhelpful to the surviving spouse and dependent children. Bank and investment accounts may be frozen. Visas may be cancelled. The home territory will be notified, which may lead to adverse results there. All because there is not a valid will. Further, depending on laws in the territory, the entire extended family may be part of the estate distribution—spouse, mother, father, children, perhaps cousins, etc. At the same time, children from a previous marriage may be disinherited. It's also likely that a greater percentage of estate assets will be allocated to pay increased expenses. Hopefully, you can see the necessity of clients having a valid will in all relevant territories, even if the estate is relatively small.

Trusts

Chapter 1 identified that not every territory recognizes trusts. Notably, civil law territories that have not signed onto the Hague Convention—the Recognition of Trusts—including several European, Asian, South American, and some other territories, do not use or honor trust documents. Where they are allowed, trusts may be used to accomplish many objectives.

Trusts are legal documents by which a person (or other entity) legally owns the property of one person for the benefit of another (Barrow, 2017, p. loc 882). The person designated as legally owning the property of the other person (grantor/settlor) is called the *trustee* and the recipient is called the *beneficiary*. Here is an illustration of a very simple trust (Barrow, 2017, p. loc 890):

> *"Mrs. B., who has a six-year old son, Timmy, is making out her will. Because it is undesirable to leave a large amount of money to a minor child, the will includes a trust for Timmy. The will may say something like, "I give and bequeath to my Trustee, John Doe, the sum of X money, to be held, administered, and disposed of as follows. My trustee is authorized to pay from time to time so much, or none, of the net income of the trust as may be advisable, in the discretion of my trustee, for the health, education, maintenance, and support of my son, Timmy. When my said son reaches the age of 25 years, my trustee shall distribute to my said son the entire balance of the trust."*

A trust will divide property into two categories: legal ownership and beneficial ownership. Legal ownership is vested in the trustee who is required to administer the trust assets (corpus), on behalf of the grantor, for the benefit of the beneficiary, who has beneficial ownership. Beneficiaries who must wait to receive the trust corpus are said to have a future interest, while those who can demand and receive current income are said to have a present interest. In the illustration above, Timmy has both a present and future interest. Additionally, the individual who receives trust assets after the trust terminates may be known as the remainderman.

Trusts may be testamentary, that is, those that become active under the terms of the will or testament, or they may be living (*inter vivos*). Technically, a testamentary trust does not exist until the grantor dies. Testamentary trusts also are funded with proceeds from the estate rather than receiving assets during the life of the grantor. A living or *inter vivos* trust, on the other hand, is created while the grantor is living. It can be funded as soon as it is created. A living trust may be revocable or irrevocable. This means that the trust may be changed or terminated (revocable) or filed in such a way that it cannot be modified or terminated (irrevocable). Legal and tax reasons may exist to choose one option or the other. An individual should exercise extreme care before arranging for an irrevocable trust, because it literally cannot be changed or terminated without the express written agreement of the beneficiary.

A grantor trust is one in which the grantor (i.e., the individual creating and supplying trust assets) retains some degree of control over the trust. He or she may be a trustee and may also be the beneficiary. A nongrantor trust is one in which the trust creator gives up all right, title, and interest in the trust corpus. Therefore, assets are entirely owned by the trust. Grantor and nongrantor trusts normally will be treated differently for tax purposes, with nongrantor trust assets being taxed to the trust.

Why would someone want to use a trust? Trusts can help accomplish many estate and legacy planning goals. As highlighted in the example above, a trust can designate a trustee who will oversee assets given to a minor child. It can also be useful when the child is not a minor, but is unable to competently manage assets. A beneficiary who cannot manage assets may not be a child, but can be a parent, sibling, or other, who may be elderly or simply unable to manage assets well. This is especially true with beneficiaries who may be physically (or mentally) disabled. Some territories allow for trusts to specifically benefit those who are disabled (e.g., special needs trust), and may provide tax or other incentives to make use of this tool. A trust may help when the grantor wishes to leave assets to a beneficiary who has drug or alcohol problems, or perhaps has a gambling addiction that has led to great loss of money and excess debts. A trust can limit access to the funds by both the beneficiary and the creditors. A grantor in a second marriage can use a trust to ensure that children from the first marriage are not disinherited.

A living or *inter vivos* trust can be funded and used to provide benefits to family, friends or others while the grantor is alive. This type of arrangement allows the grantor to have the satisfaction of seeing trust *gifts* being used by beneficiaries. It may also, as can some testamentary trusts, be used to take advantage of various taxation laws, thereby reducing the individual's current and future tax burden. Living trusts often are revocable, meaning the grantor can terminate the trust. The grantor will be unable to do this with a testamentary trust, since these are created after death. Sometimes, to take full advantage of available tax savings, a living trust must be irrevocable, meaning the grantor may not change it, and gives up all rights to the trust property.

When the grantor dies, it may be advantageous for him or her to insert a provision in the will that sends all assets (or at least those not otherwise distributed) into a trust. A will used for this purpose may be called a *pourover will*. Assets will "pour over" from the estate into the trust, and then be subject to terms of the trust. Remember, assets distributed according to terms of a will pass through probate, and that includes a pourover will.

A revocable living trust may serve in the event of the grantor's incapacity. The trust document could identify that the grantor will be the trustee during his or her lifetime. However, if the grantor becomes incapacitated, the role of trustee will be assumed by a successor, who has been named by the grantor. The new trustee will now be able to administer assets in the trust on behalf of the grantor. Use of a trust for this purpose will also allow the individual to clearly articulate the conditions under which he or she is to be considered incapacitated. We will look at incapacity in a later chapter.

Example 1		
Question		You are working with your client Mary on the design of her estate plan. Mary plans to leave all of her assets to her daughter Susan which is still a minor child of 12 years old. If something should happen to Mary before Susan is an adult, Mary is concerned about financial guardianship. Mary has a lawyer, Steve, a financial advisor Wendy, and an accountant Rhonda. Mary is financially well off but has been hesitant to create any formal structures to address this issue prior to her death. Which of the following approaches would most likely be appropriate to address Mary's concerns?
	A.	Mary could establish a testamentary trust in her will with Susan both as beneficiary and trustee.
	B.	Leave the estate directly to Susan but include directions that puts Mary's wishes in writing to Susan.
	C.	Mary could establish a testamentary trust in her Will with Susan as beneficiary and Wendy and Rhonda as joint trustees.
	D.	Establish an inter vivos trust today with Susan as beneficiary and Mary as trustee.

Correct Answer		**C.**
Explanation		This is the most appropriate type of trust which comes into being as a Will is executed, with defined beneficial ownership and legal ownership. This also allows Mary to retain charge of assets during her lifetime.
Distractor #1	**A.**	The testamentary trust comes into existence after the death of Mary. Susan as beneficiary and trustee, may still be minor in control of assets, thus a financial guardianship would be lacking.
Distractor #2	**B.**	Susan being a minor, financial guardianship is lacking in this case. Just passing on Mary's directions and wishes in writing does not alleviate Mary's concerns.
Distractor #3	**D.**	This can be a recommended course, but it comes into existence during the lifetime of Mary and needs to be funded immediately. The question says Mary is hesitant to create such formal structure prior to her death.

Determine Expenses and Estate Value at Death

The preceding content covered items that can be addressed prior to death. At the individual's death, other activities come into play. Notably, in addition to tending to all regular end-of-life activities, the individual's estate must be administered. A significant part of this process is calculating expenses, potential taxes, and determining the individual's net worth. Net worth and estate valuation must be determined, among other things, to assess taxes that must be paid. First, we will explore some of the expenses that may impact an individual's estate and its liquidity.

Estate Expenses

Final expenses can be grouped in five broad categories (Parish, 2010):

- Administrative
- Death taxes
- Debts and claims against the estate
- Cash needs
- Cash bequests

Every estate will have administrative expenses. They can be reduced by good premortem/predeath planning, but not completely removed. For example, probate court costs will be incurred, death certificates will be needed, appraisers will be required to determine property values, lawyers and accountants will be needed to address legal issues and determine estate values. Expenses will rise related to the degree of cross-border involvement. As the number of territories in which the decedent had property increases, the complexity and related administrative expenses will grow. The larger and more complex the estate, the greater administrative expenses will be.

Some territories do not levy taxes on inheritance and estate-related transfers. Others have tax structures that can be quite high. A few territories' top tax rates are 50% or higher, with one reaching 80% (Ernst and Young Global, 2017). Typically, even when the top tax rate is high, taxation fits along a range of rates that almost always start very low and increase with the size of the estate. A few territories do not have a specific estate or gift tax, but tax certain real estate transfers (e.g., stamp/transfer tax). Also, while a territory as a whole may not assess estate or gift taxes, states or jurisdictions within the territory may do so. Sometimes, the estate is not taxed, but the inheritor is taxed on all or part of the value of the inheritance. Sometimes the estate is not taxed, but gifts (lifetime) may be, or vice versa (or both may be taxed). Remember, too, while one territory may not assess taxes, another territory in which the decedent had assets may assess taxes. Usually, territories have agreements to limit double taxation, but this is not always true. Also, one territory will be named as being primary (usually the territory of final domicile). However, another territory may demand taxes to be paid on certain assets (e.g., real estate), whether or not taxes are being paid elsewhere. The potential complexity of settling multi-territorial estates is a good reason to include experts who are competent to carry out this administration.

Debts must be paid and claims settled when a person dies. This may be legally required, or simply reflect common practice. Most wills have a provision that states all debts and legitimate claims against the estate are to be settled prior to asset distribution to heirs. Some claims against the estate are not legitimate. It's not unheard of for one or more people to submit a fraudulent claim—especially on estates of the rich or famous. While the claim eventually may be denied, the process often will delay overall estate settlement, and will increase administrative expenses. There is not much that can be done to avoid this, although some trust agreements limit potential access by fraudulent claimants. The potential for having estate settlement administratively tied up is a good reason to ensure adequate liquidity in some way. One way to do this is through use of a life insurance policy paid directly to a spousal or administrative beneficiary. In most situations, policy proceeds will be paid without being subject to creditor claims or being subject to probate-related delays.

Cash—liquidity—will be needed by some of the surviving family as well as by the estate personal representative. The expenses that the family has to pay can add up quickly. Even though there has been a death, life must continue for survivors. Children continue to need food, clothing and shelter. The funeral must be arranged and paid for. Debts must be paid. In other words, all normal expenses continue, and end-of-life specific costs require money. It's not uncommon, if death is preceded by a significant illness, for medical expenses to add up. Any of these in excess of state social security benefits or insurance must be paid. Additionally, settling the estate often requires payments of fees and taxes. Appraisals cost money, and appraisers don't want to wait until the estate is settled to be compensated. The same is true with lawyers, accountants, and others involved in settling the estate. As a general rule, a well-thought-out, well-constructed estate plan, with appropriate legal documents, can reduce administrative expenses and related liquidity needs. Being required to sell assets to pay expenses is almost never a desirable course of action. Asset sales as a result of death often bring lower prices than might otherwise be the case. This is especially true when a sole proprietor's or partnership business must be sold (a good reason to have a buy-sell agreement in place). Real estate sales also often suffer when potential buyers realize the property is being sold to provide the immediate need for liquidity. Once again, a life insurance policy with a properly designated beneficiary can help avoid at least some of these situations. As a possible solution, assets can be sold or gifted prior to death so there can be cash on hand as it is needed. However, remember that assets that pass at death sometimes receive better status for tax purposes than cash or cash equivalents. As a financial planner, you will want to discuss options, implications, and trade-offs with clients, in coordination with an estate planning expert.

Cash bequests may be less urgent, but they increase the need for estate liquidity. It's probably a good idea to limit or eliminate entirely any cash (as opposed to property) bequests. This will help reduce estate liquidity needs.

Determining Estate Value

We have looked at some of the expenses and contributing factors that may impact an estate. These ultimately must be subtracted from the estate's value. The estate's value has several components that include the gross estate, probate estate, and taxable (net) estate.

The **gross estate** is everything owned by the decedent. This can include all current assets, bank and investment accounts, at least some portion of jointly held assets, amounts owed to the individual, but not yet paid, ongoing royalties, real estate rents[17], retirement accounts and similar continuing income streams, life insurance payable to the estate and some policy situations where the decedent retained incidents of ownership (even when the proceeds go to a named beneficiary), revocable living trust assets, trust assets where the decedent was the beneficiary, real property, and business interests. Assets jointly owned with a spouse may be assessed at half the current market value. Other jointly held ownership arrangements will be assessed based on the percentage contribution of each owner. So, if the decedent owned 60% of a property, that's the percentage of the value that will be included in his or her estate. If the decedent owned an asset and controlled it, the asset can be a part of the gross estate[18]. To determine the value of a gross estate, add the value of all assets in which the decedent held incidents of ownership.

The **probate estate**, in contrast, includes only those assets that pass through probate. This means assets distributed according to a will or by the rules of intestacy. It does not include assets, such as will substitutes, which can include life insurance to a named beneficiary, irrevocable trust assets, certain ownership titles, and other assets that pass according to law. The probate estate will often be smaller, sometimes quite a bit smaller, than the gross estate.

The **taxable estate** will vary based on includible assets, which varies by territory. As we have mentioned, some assets may be assessed at higher rates than others—notably real estate. A territory may have tax rules that eliminate the value of some assets from taxation. Certain ownership provisions (e.g., how an asset is titled or owned) may reduce or eliminate potential taxes. Some assets are legislatively carved out of the taxable estate. Cross-border estates likely will experience taxation at different rates, perhaps on different assets. It's possible that a separate accounting will be required for each relevant territory. Doing this can get tricky when certain assets, such as ongoing retirement income streams or other investment-generated unearned income streams, are part of the mix. One of the questions that must be asked is who has jurisdiction. The answer will depend on the way taxes are assessed by applicable territories and the treaties in effect that reduce or eliminate double taxation. Often, an ongoing income stream is deemed the purview of the territory in which it is generated. This may result in taxation (income or estate) in that territory in addition to the country of last domicile.

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[17] It may be necessary to determine the value of a piece of commercial real estate using an evaluation method such as the gross income/rent multiplier or net operating income capitalization. These calculations were presented in FPSB's Investment Planning and Asset Management course.

[18] This is a reasonable working definition of *incidents of ownership*. A person may own an asset or control its use, even when it has been placed in trust or given as a gift. An outright or completed gift is one where the owner gives total control to a new owner. Contracts, such as life insurance policies, in which the policy owner has the ability to determine beneficiaries, take policy loans, or impact the policy in some other way qualify as having incidents of ownership.

From the gross estate, subtract any amounts carved out by legislation (e.g., assets going directly to a spouse). Also, subtract debts and other expenses, which may include funeral expenses, excess medical bills, administrative expenses to settle the estate, outstanding mortgage, and other debt amounts that must be settled. Determining the value of an asset may require professional appraisal. Related expenses qualify as an administrative expense. The amount that remains is a net estate. Some territories exempt the value of certain assets, especially those going to a spouse or perhaps children, from taxation (or tax those assets at a different rate). After subtracting all debts/expenses, nonincluded assets, and exemptions, what remains is the taxable estate. Remember, taxable amounts may vary in different territories as the estate is assessed; especially relevant in cross-border scenarios.

Ways to Reduce Taxes and Expenses at Death

Expenses reduce the gross estate, thereby reducing the net or taxable estate. While it's nice to lower the tax burden, we want to make sure that assets pass according to the wishes of the decedent and aren't used for more expenses than necessary. Therefore, reducing expenses is almost always a viable estate planning tool. We will look at a few ways to reduce at least some related expenses.

Administration

Even estates with little financial value require some degree of administration, which will add to end-of-life expenses. Three potential areas can increase administrative expenses: probate, assessment and valuation, and litigation.

Probate

Probate is the process of administering estate assets that pass according to a person's last will and testament. Probate also reviews a will to determine whether it is valid. Individuals who die intestate will have their estate administered and distributed via the probate process. The court will appoint a personal representative (as named in the will) or an administrator for estates with no valid will. The probate court also will mandate payment of any taxes and outstanding liabilities from the decedent's estate. Probate costs money—court costs, lawyers, research, notification of heirs, meetings with interested parties, and the like. The more ambiguous the estate documentation, the more probate will cost. The probate process does not apply to assets that pass apart from a will or intestacy statutes, or by will substitutes (e.g., life insurance to a named beneficiary) or by law (e.g., joint tenancy held/titled assets)[19]. However, when probate applies, it makes sense to limit related expenses when this is possible.

A simple way to make probate less expensive is to have a well-written, current, valid will that provides all the direction needed to administer the estate. This will result in less need for research—trying to locate heirs, find property specifically named in the will, identify valid liabilities, etc. Less research means lower expenses. A well-written will should identify all beneficiaries and the assets (or percentages of estate value) assigned to each. The will must comply with relevant laws and clearly articulate the decedent's distribution wishes, all in accordance with laws in the territory around mandatory succession (inheritors/heirship). Most territories have succession laws protecting a

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[19] Territories that follow English common law may identify the probate process as a *grant of representation*.

surviving spouse and/or children so they cannot be disinherited, regardless of provisions to the contrary in the will. Cross-border situations increase expenses—especially when real estate/property is included—and there is little that can be done to change this. However, when the decedent ensured that there is a current valid will for each applicable territory, estate administration expenses will be minimized.

Appraisal and Valuation

All assets do not have to be valued, but many will require an appraisal to determine current valuation. Determining the value of the gross and taxable estate is one reason for this. Another reason is to pay relevant income or other inheritance-related taxes (in addition to general estate tax). When an appraisal is required, it will be done through the services of a professional appraiser, likely appointed or approved by the court. The more complex the property, the greater the related appraisal fees. Some items, such as collectibles, may require an appraiser with specific expertise. The same likely applies to real estate, especially commercial (i.e., income generating) properties. More than one appraiser also may be required to accurately assess the value. The personal representative should determine the degree to which an appraiser is qualified and authorized to do the appraisal. In many places, appraisers are required to have completed relevant training and to be appropriately licensed. Variations in an asset's valuation normally can be rectified by obtaining more than two appraisals. Unfortunately, appraisals will increase expenses, but doing so normally will be worth the cost.

Litigation

Sometimes people who are related to the decedent in some way are not pleased with the intended distribution plan. Perhaps they did not receive one or more assets they believe they should have. Maybe they were completely disinherited and feel they should not have been (e.g., children from a former marriage, adopted children, people to whom the decedent may have made a promise related to distribution, etc.). When this type of situation arises, it may be settled amicably without judicial intervention. However, often, the court is brought in to make a determination as to the validity of the original distribution plans and claims against the estate. Courts have fees and lawyers must be paid, so litigation can be expensive. In fact, in some situations, litigation becomes one of the more onerous estate settlement expenses. Clarity in the will can help, but likely will not eliminate all potential litigation. Sometimes, the decedent was not completely competent and may have made statements to one or more individuals that were inconsistent with provisions of a written will. These statements may or may not represent a legitimate bequest, and often will be quite difficult to litigate.

Royalties from, and ownership of, intellectual property can be especially difficult to administer. One reason for this is that multiple parties may have had a hand in creating (and bringing to market) the intellectual property, but all parties may not have been included in its testamentary distribution. Thinking of possible related expenses, consider a situation where potential contributors or partial owners live in multiple territories, or perhaps some distribution rights to the property have been licensed in various places. Especially when the value is high, each of these potential litigants will require legal representation along with defense by the estate, all of which will be expensive. Lack of clarity in the decedent's desires is a main cause of estate disputes, but is not the only factor. Especially when children are involved, and more, when the children come from more than one set of parents, guardianship can become an issue. Guardianship usually includes some degree of financial remuneration, and also may involve administration of children's assets. Small estates may be simpler to determine than large estates, but disagreements among family members can be heated in any size administration. This seems to especially be the case when the decedent was famous and likely wealthy. Some cases drag on for many years, with no side wishing to give way on their claim. If you happen to be the financial planner involved in such an estate settlement, your participation may become much more involved than you originally anticipated. You also may become enmeshed in the legal process, which, in turn, may require you to retain legal counsel for your own benefit.

Debt, Tax, and Other Financial Settlement

Settling debts and paying taxes are part of overall estate administration. It's worth exploring the topic separately, in part, to look at ways the financial aspect of this area can be minimized. One important factor to keep in mind is that not all debts must be settled at death. Sometimes, such as when a mortgage or other loan is jointly held, the remaining debtor can continue making payments, rather than pay off the entire loan immediately. Likewise, depending on rules within different territories, credit debts held solely by the decedent may not have to be repaid by survivors (but the estate may be liable). Survivors might decide to do so, but may not legally be required to settle all the decedent's debts. The personal representative or the courts should make this clear to surviving family. Some debt settlements may be negotiated by the surviving family to reduce overall amounts or extend repayment periods. Both options are worth exploring.

The taxable estate is based on the gross estate after subtracting all applicable expenses. Since the taxes are due to be paid to the government, amounts generally are what they are. Although specific property valuations may be adjusted or determined as of a date following death (when the evaluation is more favorable), when the final tax bill is determined, it must be paid. The taxation process may include multiple territories, and it's worth checking on double-taxation treaties and potential credits or exclusions.

The specific date investment holdings and real estate property are settled can make a difference in the valuation. Markets constantly are in flux, and account (and property) values change daily. It may be possible to pick a date that is more advantageous than the date of death for determining account values. Consider a situation where the stock market is dropping. For taxation purposes, a delay in settlement can result in a significant devaluing of the portfolio. This will lower the taxable estate, but probably will not decrease long-term valuation of the inherited portfolio (both of which are positive outcomes).

One way to decrease estate taxes and administrative expenses is to remove assets from the estate prior to death. Generally, this is accomplished by making one or more (completed) gifts. The gifts may be outright and direct or via trust. Some territories provide special exemptions and credits for gifts to charitable organizations. Where possible, this has the positive result of supporting the charitable organization as well as reducing estate taxation and settlement expenses. Similar results can be achieved with most lifetime gifts. Gifts must be deemed as being complete, meaning the owner completely releases legal and beneficial ownership of the asset. In some scenarios, in certain territories, a grantor can place gifted assets in a charitable trust, with the charitable organization named to receive full ownership at some point in the future. In return, the charitable organization provides the grantor with a degree of income from the asset for a period of time. The gift is deemed as being complete and removed from the grantor's estate, but he or she receives ongoing benefit in the form of an income stream. Another example might be when a parent gifts a house to a child but retains the right to live in the house for a period of time. At the end of that predetermined period, full ownership—

beneficial and legal—passes to the child. In the meantime, the parent continues to have a place to live.

The preceding provided some examples of life transfers of property (i.e., gifts). The next chapter will explore this topic, along with transfers at death, in more depth.

Discussion Questions

Chapter Review

1. What are common steps that should be part of most estate plans?
2. When creating an inventory, in addition to identifying property, what types of things should the list include?
3. What are four basic coverages of a will?
4. In most territories, how may a will be used to disinherit a surviving spouse and/or children?
5. What is a residuary clause, and why would one be included in a will?
6. How likely is it for a will drafted in one territory to be completely valid in another territory (i.e., cross-border scenarios)?
7. How does a trust divide property ownership?
8. What is a grantor trust and how does it compare to a nongrantor trust?
9. How may a trust be used to benefit a minor beneficiary or one who is unable to competently manage assets?
10. What is a pourover will and how might it be used?
11. Final expenses may be grouped into five broad categories. What are they?
12. Why is cash (liquidity) needed by survivors?
13. How is the value of a gross estate determined?
14. How does the probate estate differ from the gross estate?
15. What is the taxable estate and how might it be settled?
16. Must all debts be settled (fully paid) at the death?

Chapter 4: Transfer During Life and at Death

Learning Outcomes

Upon completion of this chapter, the student will be able to:
4-1 Describe estate distribution/transfer tools
4-2 Distinguish between testamentary and *inter vivos* transfers
4-3 Describe laws of succession and compulsory (forced) heirs

Introduction

Estate-related transfers may be made during life or after death. Lifetime transfers are called gifts and also are known as *inter vivos* transfers. From the Latin, *inter vivos* means between living persons, and may be done via a trust or outright. Transfers at death may be testamentary, i.e., according to terms of a decedent's will. Transfers also may be made subject to laws of intestacy. Similarly, property may be distributed as required by law or via one or more will substitutes. We will explore lifetime gifts first, then look at transfers as a result of death.

Lifetime Transfers

Lifetime, or *inter vivos*, transfers may have a primary purpose of removing assets from an estate. However, many times, an equally strong reason to make a gift is the giver's desire to see the recipient use the gift. The recipient may be a family member, friend, partner, charitable organization, alma mater, or other. Often, individuals—especially high net worth individuals—choose to give a gift while living to help the recipient in one way or another. A gift to an alma mater might come in the form of establishing a scholarship for students or perhaps endowing a research chair or having a building erected on campus. A gift to a family member might help him or her purchase a home, start a business, pay off debt, start an investment portfolio, support children or grandchildren, pay medical expenses, or simply improve their financial well-being. A charitable organization may receive a gift and use it to carry on one or more charitable projects or support the organization so it can, in turn, support others. Gifts may be made to accomplish many objectives, only some of which are specifically financial.

Regardless of intent, either the gift-giver (i.e., donor—typically) or recipient (i.e., donee—occasionally) may incur a tax on the value of the gift (i.e., where no money is received in return for what is given). Not all gifts are taxable. For example, a gift to a recognized charity is exempt in some territories (Old Mutual International, 2017). Gifts may be considered exempt, potentially exempt, or a fully taxable/chargeable lifetime transfer (CLT). Many territories have a *lookback* period for when the gift giver dies within a certain period of years following the transfer. For example, the value of all gifts made within three years (or seven or other) of death may be recalled to be part of the estate valuation. Usually, a certain amount will be exempt from taxation regardless of the recipient. Likewise, gifts to a spouse or civil partner may well be exempt from taxes in full or part. Also, very small gifts often may be made with no tax implications.

A number of territories have a unified gift and estate/inheritance tax. Where it exists, the tax applies to the value of the estate at death and to certain transfers or gifts made during the individual's lifetime (Ernst and Young Global, 2017). Where taxation exists, some amount of valuation often is exempt from taxation. For example, a $5 million estate value may be reduced by $3 million as a result of a legislative exemption/exclusion. The remaining $2 million will be subject to taxation. In a unified system, the value of lifetime gifts will be deducted from any estate tax exemption. As a result, it may be possible to give lifetime gifts with enough value that there is no estate tax exemption/exclusion left, and the entire taxable estate actually will be taxed. Quite a few territories have eliminated both gift and estate/inheritance taxation, but some of these may levy a type of stamp or income tax instead.

To determine the taxable value of a gift, first consider whether the gift is subject to taxation. Some territories eliminate charitable gifts, gifts to immediate family (especially spouses/partners), and very small gifts from taxation. If a gift is potentially taxable, look at whether any reduction in value via appraisal, depreciation, or other, may be applied. From there, apply exclusion/exemption amounts. Taxable gifts must be reported on the appropriate forms and tracked so exemptions, etc., can be appropriately applied. Taxes may be applied to property transfers within a particular territory only, or on a worldwide basis. This is true for gifts as well as for estate (i.e., at death) transfers. Further, citizens and noncitizens may be taxed at different rates and have different exemptions or deductions.

Small Business Owners

In Chapter 2 we covered disposition of an interest in a small business at the death of an owner. Especially when the business is structured as a sole proprietorship (i.e., one owner) or partnership with two partners, selling the business after the owner (or one of the two) has died can result in having to sell at a deep discount to the anticipated business value. It may not seem fair, but often, when a potential buyer knows the surviving family must sell the business, he or she will demand a discounted sale price. If the family feels compelled to sell so they can gain necessary liquidity (e.g., to pay inheritance taxes or support cash flow needs), the buyer probably will get the discounted price. Having a buy-sell or business continuation agreement funded with life insurance is one way to address this problem, but it most likely will not be possible with a sole owner (i.e., there may be no one willing to enter into the *buy* side of the agreement).

Another possible solution is for the owner to sell (e.g., as a going concern) or liquidate the business prior to death. This could be done as a transfer for value (e.g., purchase price = business's appraised fair market value), or when appropriate, the owner might make a gift of the business. When making a gift, the most likely (but not the only possible) recipient will be a family member. Gifts to family will be subject to the territory's normal gifting rules, including potential taxation. If the owner *sells* the business to a family member at a discount, the difference between the discounted price and fair market value likely will be deemed a gift, and taxable to some degree. The same probably will be true for any advantageous transfer methods used (e.g., discounted loan, favorable installment sale terms, etc.). One of the questions the owner and family member recipient must ask is whether the recipient is willing and capable of running the business. If not, an outright sale to a third party probably will be a better solution.

If the sole proprietor decides to gift the business to a family member, he or she may also want to shift the form of ownership to create different classes of ownership interest. This may mean (for example) reorganizing as a partnership or becoming a closely held corporation that can issue stock. Doing this will allow the owner to gradually transfer ownership, while maintaining a degree of control during the transfer period. One possible arrangement would be to create two classes of stock: common and preferred. Common stock has voting rights and could remain with the current owner. Preferred stock normally has no voting rights and could be gifted to the family member.

Alternatively, the family member could be given a nonmajority share of common stock, and the current owner could keep preferred stock as a way to guarantee ongoing income. (Holders of preferred stock must be paid all dividends/income due them prior to the corporation paying any dividends to other shareholders.) This would begin the transfer process, reduce financial exposure to the owner's estate, and allow continued control of the business by the current owner.

Actual gifting of the business could be accomplished all at once, or over a period of years, depending on which option works best in the overall plan (especially if there is an annual exclusion on gift taxation up to a certain limit). It may be possible to divide the gifts in such a way that they do not trigger any taxation, nor do they reduce available exemption amounts. Any gift tax will be based on the pre-gift fair market value after subtracting the amount of ownership percentage/value kept by the donor. This can be a somewhat speculative process for non-publicly traded business shares, but normally it is possible to get a professional appraisal of the business value. The process is simplified if corporate shares are traded on a public market, because the value can be established by multiplying current price per share by the number of outstanding shares. All the other normal options for valuing a business may also be applied. Often, but not always, the donee is able to carry over the basis from the donor. Gifting a business to one or more family members, especially if accomplished over a period of time, can increase the donee's interest in and ability to manage the business. This will allow the donor/owner to have greater confidence that the business will continue operating successfully.

Transfers at Death

So far we have discussed *inter vivos* transfers as well as those that happen as a result of death. In this section we can add a few details to deepen understanding of the process as it relates to transfers following death. To begin, a person who has died cannot continue holding onto owned assets. As a result, the decedent's assets must be distributed to someone. It is most helpful when the decedent has addressed his or her distribution wishes prior to dying, but this does not always happen. In the most disadvantageous circumstance, the decedent will not have made any distribution arrangements, and the state must step in to determine appropriate distribution. As mentioned earlier, when an individual dies without a valid will, he or she is said to have died intestate. When this happens, legislative rules of intestacy govern the estate distribution. Intestacy laws vary from territory to territory, and sometimes, by region, state, or province within a territory. We have looked at intestacy already, so we will summarize key points here.

Personal Representative

To begin, whether or not a decedent has left a valid will, the estate distribution process will require a personal representative (PR—also known as an executor/executrix or administrator). A well-constructed will should name the PR, who the court can approve, but when the individual dies intestate, the court will appoint a PR or administrator. It's possible that the person appointed or named in a will declines to serve. When this happens, the court will seek the next most competent individual to appoint. Sometimes this may be the surviving spouse or other family member. If no one can be found to serve, the court may appoint a local lawyer or bank. Whoever is chosen as PR will be given legal authorization to represent and act on behalf of the estate.

One of the first duties of the PR is to determine (and seek out) the decedent's assets. This means the PR may need to contact banks and financial institutions and notify them of the person's death. He or she will also provide authorization to become the legal point of contact moving forward. During this part of the process, the PR will need to collect any money held in accounts solely titled in the decedent's name. The PR will also want to ensure the decedent's real and personal property (e.g., house, use assets, cars, etc.) are protected as much as possible against the possibility of theft or vandalism. Depending on the way property is titled (e.g., tenants in the entirety, joint tenants with survivorship rights, etc.), full ownership may immediately shift to the surviving partner or other owners. It then will become their responsibility to protect, insure, and maintain the house (or other property).

The PR will collect amounts that may be due the decedent. This can include rents, royalties, debt repayments, and the like. He or she also will need to contact sources that provide ongoing income streams (e.g., social security, pensions, deferred payments from employment, etc.) and inform them of the death, along with any change in payment information. This may include life insurance payments that should be made to the estate (but not those going to a named beneficiary). The PR will be required to act in the interest of the decedent's estate and most likely will have to give a report to the court on those actions.

The PR will need to ensure that required debt and other payments owed by the decedent get paid as agreed. He or she must notify creditors with all relevant information, including instructions for filing a claim against the estate. A related function is to determine, and make payment of, taxes that are due. Doing this will take a little time, because there is a lot that must happen prior to filing final tax forms (including all that has already been mentioned). The PR will have to discover gifts that have been made and whether they will impact available exemptions or deductions. It's unlikely the PR will prepare the final forms; this normally will be done by an authorized accountant or similar. The PR may have to get necessary assessments to determine asset values and liabilities, identify valid expenses, and provide any other information that will be required when filing final forms.

The PR may be required to administer estate assets until they are distributed to heirs. This may include maintaining adequate insurance, managing investment portfolios and real estate properties, overseeing business operation or disposition, and protecting estate assets to the degree possible.

Finally, the PR will distribute assets according to terms of a valid will or applicable statutes. This may include adjustments to and delivery of property deeds and certificates of title, documents authorizing assignment to appropriate heirs, checks for cash bequests, and transfers of investment and bank accounts. The PR also may be required to distribute assets according to forced heirship, spousal rights, or other territorial statues. It's possible that one or more lawsuits may arise, and the PR may have to participate in at least some of these.

Assets that pass by law or by will substitute make the PR's job a little easier, because distribution is mandated by applicable laws. However, this may get a little tricky when the decedent left a will that, for example, disinherited a spouse or children, because the law seldom allows this to occur. In these situations, the court will have to rule on how the final distribution is to be made.

Probate Process

Much of what has been discussed so far includes probate. Probate is the orderly process of estate distribution according to a valid will or applicable statute (e.g., rules of intestacy). It is handled through a probate court (which may or may not hold that title, depending on the territory). Probate has some negatives, but there are several positives, too.

Probate is fair and orderly. The probate court oversees the process, which provides boundaries and structure. It also ensures fair distribution of assets according to the valid will and/or applicable statutes. Anytime one or more heirs has a disagreement as to the proposed distribution, the court will hear the dispute and make a ruling. Doing so may take time, but in the end, a *disinterested, unbiased third party* will have made a ruling that is as fair as possible. The process also is structured according to relevant laws and applicable rules. This helps to keep things moving forward in the most effective, efficient manner. Probate provides a venue for heirs to receive valid titles and other forms showing a change in ownership. It also gives creditors a venue to ensure legally valid claims are honored. Payment of taxes also is a part of the process.

There are some downsides to probate. First, probate can be expensive. All the court costs, legal fees, assessors, accountants, the personal representative, and related fees can cost a lot of money. These expenses are paid prior to distribution of assets and may result in a smaller estate to be distributed. As a result, most people want to keep the probate process and its expenses to a minimum. Also, probate takes time; the process of determining asset values, applicable heirs, etc., can be time-consuming. The resulting delay in distribution can become frustrating for heirs. Probate records generally are considered public information. This means interested parties can access much of the information and make it public. Many times this will not be an issue, but especially for estates of famous people and the very wealthy, it can be a problem.

High Net Worth Individuals

Estate planning for high net worth individuals (HNWI) is not fundamentally different from estate planning generally. HNWI most likely will want to ensure that taxes are minimized, probate is avoided, and inheritance rights for their chosen heirs are protected. When estate taxes apply, estates of HNWI are almost certain to be impacted with a higher than average tax burden. It makes sense that they would want to take advantage of any exemptions and deductions to reduce taxes, thereby increasing assets available to pass on to their spouse, children and other heirs.

In addition to avoiding the costs of probate, many HNWI individuals would prefer to keep their information, especially their net worth, private. Probate makes a lot of information available to the public. Net worth and the amount of assets distributed to heirs is among the possible public information. This can be exploited, and it's easy to understand why HNWI do not want this to occur. As a result, they are more likely to make transfers via one or more trusts (*inter vivos* and testamentary) and during their lifetime (i.e., gifts).

Unscrupulous individuals can try to get at assets in anyone’s estate, and especially those of HNWI. They can pose as creditors, present high-return, high-security investment plans, and otherwise try to get heirs to give them as much of their inheritance as possible. Remember, people dealing with the death of a close family member often are not as emotionally or mentally stable as usual. They are processing their loss and grieving. This process can make it difficult to think clearly and rationally. With their increased (albeit temporary) vulnerability, it can be relatively easy to take advantage of them. Of course, heirs of HNWI make more lucrative targets than those with fewer financial assets. To protect against this, HNWI may find it reasonable to have assets flow into a trust and name a reliable, often professional, trustee. Additionally, they may use foreign (e.g., offshore) corporations to hold assets, or perhaps make use of domestic corporate (or other) entities that provide a degree of security and privacy. One of the reasons this can work is that the heirs don't actually own the assets—The corporation (or other entity) does. Proper documentation ensures the heirs access to the assets, and they will be protected from predatory individuals in the process. The exact company structures and trusts used will vary by territory (because different territories only acknowledge certain structures and trusts), but the concept is valid most places.

Forced Heirship

A will can accomplish many things, but seldom can it overrule territorial succession statutes and mandatory distribution laws. Not all territories embrace the practice of forced heirship. In certain cases, a will may override some of the statutes, but seldom can it overcome all of them. When there is no will, intestate succession will follow forced heirship when it is applicable.

As the name implies, forced heirship means a decedent is not free to distribute the estate in whatever manner he or she desires. There are strict rules to be followed identifying who must inherit assets, based on what percentages. Forced heirship rules are only occasionally found in common law territories, and are often found in territories following civil law, including many Arab (Islamic) states and territories in Europe, Japan, Latin America, and Russia (CFA Institute, 2017). The rules vary and may or may not provide support for a surviving spouse. Children (protected heirs) almost always are provided for. In several situations, providing for the children (and perhaps grandchildren) may mean that the spouse effectively is disinherited. At best, the spouse—often the wife—may receive only a nominal share of the estate. We should reinforce that not all forced heirship regimes effectively disinherit the surviving spouse. However, it happens enough to be a potential concern for the spouse. Mandatory heirs may extend beyond immediate family members to include parents, grandparents, siblings, cousins, and other related persons. Some forced heirship scenarios allow for a *disposable/discretionary* or free estate share that can be distributed according to the decedent's desires, and so estates are divided between a forced heirship (hereditary reserve) portion and a discretionary portion.

Generally, there is an order to how inheritance is distributed. The first, and largest share often going to the first-born (often male), then to the next in line, and so on. It's possible that, under such a plan, those in a lower category may receive no inheritance, as the assets will have been fully distributed (Skandia International, 2008). While forced heirship may or may not seem fair, it does have at least one beneficial aspect: Costs, especially from legal challenges, are minimized.

Three primary options exist that may circumvent forced heirship estate distribution. The first is through making lifetime (*inter vivos*) transfers. Usually, a period of time must pass between giving the gift and death (e.g., 10 years), otherwise, the gift may be challenged and recalled (Skandia International, 2008). Lifetime transfers work because any assets that are gifted (following proper procedures) are no longer are part of the estate, therefore, at death, it's not possible for them to be included in a forced heirship scheme. A second option is to create a trust (*waqf* in Islam). Though not all territories recognize trusts, it may be possible in some territories to circumvent forced heirship rules by using a trust. The trust can nominate beneficiaries who, as legal owners, will receive trust assets, bypassing forced heirship distribution. Some territories, however, specifically deny the right of a trust to bypass the heirship rules. A third possibility is to establish a foreign company to own property. Property transferred to a foreign company (e.g., offshore) is likely not to be impacted by a territory's forced heirship rules.

A number of forced heirship systems do provide a significant portion of the marital estate to be distributed to the surviving spouse, but the spousal portion may be reduced to provide for children. Often, the spouse's share may be 50% of the estate, or at least the community property portion is provided to the spouse. Community property is marital property. The exact definition and usage varies by territory, but essentially, marital assets are considered to be jointly and severally owned by spouses. The origin of community property concepts is debated, but its purpose generally is agreed. It provides a degree of security for the surviving spouse (especially the wife) (Dué, 1964).

A related concept—*usufruct*—is not often found in English common law systems but is more prevalent in civil law territories. Usufruct technically refers to the ability of a person to use the property of another person, without changing the character of the property. It may be applied to use of land, buildings, and/or movable objects. In some circumstances, it can even extend to using money and other assets that may be totally consumed by the user (i.e., usufructuary). Usufruct is not specifically limited to surviving spouses, but it can be applied for their benefit. Usufruct can allow a surviving spouse to live in the family home, use community property assets, and the like. The right normally terminates at the earlier of remarriage or death. As such, usufruct is not necessarily as beneficial as outright inheritance and ownership, but it does provide a degree of security to the surviving spouse.

One of the concerns faced by many people, especially the elderly, is the possibility of incapacity. This may be physical, mental, or a combination of the two. Regardless of the specific circumstances, incapacity can disrupt the incapacitated, the lives of those around the incapacitated person, and bring long-held plans to a halt. We will explore incapacity in the following chapter.

Example 1		
Question		Probate is the orderly process of estate distribution according to a valid will or applicable statute (e.g., rules of intestacy). It is handled through a probate court (which may or may not hold that title, depending on the territory). Probate has some positives. Which is of the following is least likely a positive regarding probate?
	A.	The probate process is structured according to relevant laws and applicable rules. This helps to keep things moving forward in the most effective, efficient manner.
	B.	Porbate ensures fair distribution of assets according to the valid will and/or applicable statutes.
	C.	Probate is not expensive.
	D.	Probate is fair and orderly. The probate court oversees the process, which provides boundaries and structure.
Correct Answer		**C.**

Explanation		Probate can be expensive. All the court costs, legal fees, assessors, accountants, the personal representative, and related fees can cost a lot of money. This is a downside or negative to probate.
Distractor #1	**A.**	The probate process is structured according to relevant laws and applicable rules. This helps to keep things moving forward in the most effective, efficient manner.
Distractor #2	**B.**	Porbate ensures fair distribution of assets according to the valid will and/or applicable statutes.
Distractor #3	**D.**	Probate is fair and orderly. The probate court oversees the process, which provides boundaries and structure.

Discussion Questions

1. Why would an individual want to make an inter vivos transfer rather than a transfer at death?
2. How and why might a small business owner make a gift of the business to a family member?
3. What are the responsibilities of a personal representative (PR) and how do they impact estate distribution?
4. Why would an HNWI want to avoid the probate process as much as possible?
5. What potential concerns are created by a forced heirship regime? What are some methods to address the concerns?

Chapter Review

1. What are two primary reasons for making an *inter vivos* gift/transfer?
2. Who normally pays taxes related to giving or receiving a gift?
3. If an individual wants to reduce estate-related liabilities by giving an *inter vivos* gift, is there any possibility the gift may be recalled or brought back into the estate?
4. What is a unified tax and how may it be applied?
5. What are some of the options a sole business-owner may use to transfer/distribute a business interest while he or she is living?
6. What are some available stock-based options for a sole proprietor who wants to gift a business to a family member?
7. What is a personal representative (PR) and what are some of his or her primary functions?
8. Probate can be a positive process used to effectively administer a decedent’s estate. However, it also can have some negatives associated with it. What are some of the negative aspects of probate?
9. What options may HNWI and heirs use to protect their privacy as part of estate distribution?
10. What categories of family members may be considered mandatory heirs in a forced heirship scheme?
11. Three main options exist that may circumvent forced heirship distribution schemes. What are they?
12. What is usufruct and how may it apply to estate planning?

Chapter 5: Planning for Incapacity

Learning Outcomes

Upon completion of this chapter, the student will be able to:

5-1 Describe incapacity
5-2 Analyze plans to address incapacity

Introduction

Incapacity[20] may be defined as having a lack of capacity. When an individual suffers from an incapacity, he or she has a disability—physical or mental—that impedes the ability to think and act as desired. Incapacity also can make a person legally ineligible to handle their own affairs. This most often is caused by experiencing a lack of mental fitness. The person is unable to process information appropriately or understand the consequences of their actions. When a person is judged to be incompetent and has not made prior arrangements, a guardian or administrator often is chosen as a helper, and this arrangement may not be wholly satisfactory to the individual. The state will make decisions on behalf of the individual and do so by following predetermined guidelines. This may result in loss of personal freedom, which may include having a caregiver put in charge who is unknown by the individual or the family. Sometimes, in the legal realm, the incapacitated person no longer has the right to represent themselves. This is disruptive to the individual, as well as for close family members. There can be many implications, but one thing is certain: Life, as previously known and experienced, will be changed, perhaps permanently. There are ways to keep many of the effects from taking over, and this type of preplanning can yield beneficial and desirable results.

Many people struggle to plan for potential incapacity. One simple reason being, they never consider that it could happen to them. If they currently have full control of their mental and physical capabilities, why would they believe that might change? As their financial planner, you can provide a valuable service by educating clients about the potential for incapacity and what they can do to prepare in the event it impacts them (either directly or via a dependent or family member). Another reason people may not plan for incapacity is that doing so is not all that pleasant. Many people get at least a little uncomfortable considering a time when they no longer maintain enough control to effectively manage their own affairs. Nonetheless, incapacity is a fact of life for many, and likely will continue, especially as the overall population grows older. It may be a difficult conversation, but it's an area financial planners should cover with clients.

Degrees of Incapacity

Incapacity may be temporary. A person who undergoes surgery may temporarily be incapacitated while recovering. After recovery, the individual goes back to a more typical life experience. At the other end of the spectrum, dementia and other types of cognitive impairment may be permanent and render the individual unable to interact effectively with the surrounding environment.

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[20] This section will focus on mental incapacity as being the more applicable to course coverage. Physical incapacity also can be significant, but especially for the elderly, mental incapacity is likely to have a greater impact on estate planning. Although incapacity can impact any person of any age, we will focus on the elderly (while remembering that much of the coverage is applicable to minors as well as adults).

Mild Cognitive Impairment

Mild cognitive impairment (MCI) causes a slight, but noticeable and measurable decline in cognitive abilities, including memory and thinking skills (alz.org, 2017). While the impairment is noticeable to the individual along with close family and others, it does not interfere with the ability to carry on with daily life. Sometimes, MCI can revert to a more normal state, but other times, it progresses to dementia (alz.org, 2017). Aging is not the only causal factor, but it is perhaps the most common and significant. One of the main MCI concerns relates to whether it is remaining stable, moving back to a more normal state, or heading into full-scale dementia. This is why it's important to correctly recognize and diagnose MCI, and for the individual and those close to the individual to keep watch. According to the Alzheimer's Association, a medical workup for MCI can include the following core elements (alz.org, 2017):

- Thorough medical history
- Assessment of independent function and daily activities
- Input from a family member or trusted friend
- Assessment of mental status
- In-office neurological examination
- Evaluation of mood (especially to detect depression)
- Laboratory tests (perhaps including brain imaging)

Symptoms of MCI can include (Mayo Foundation, 2017):

- Forgetting things more often
- Forgetting important events such as appointments or social engagements
- Losing a train of thought or conversation thread
- Feeling overwhelmed by decision-making, planning steps to accomplish a task or interpreting instructions
- Having trouble finding the way around familiar environments
- Becoming more impulsive or showing increasingly poor judgment
- Family and friends notice these changes

As a financial planner, you cannot do an analysis, but when working with a client, you may notice some signs of MCI. If you do, you can suggest to the individual, and perhaps a trusted family member or other individual, that an evaluation, including some or all of the above, might be beneficial. When a client experiences mild or full-scale dementia, it will change your relationship with them—both legally and professionally. If you do not identify suspected incapacity to appropriate individuals (e.g., family, supervisors, related professionals), you may become legally liable for your actions. This is especially true if you are deemed to have taken advantage of the diminished mental capacity of the individual. Further, as a trusted advisor, you may be able to alert the client and/or family to a condition that has the potential to become critically disruptive.

Transitional State

An individual sometimes may change directly from full cognitive capacity to being entirely impaired cognitively. Often, though, there is a period during which the individual moves between the two states. The period can be short or may take a number of years. Often, it begins as the individual ages, but may commence earlier in life. For our purposes, the significance of a transitional period is to recognize an increasing amount of cognitive dissonance and inability to continue functioning in a normal capacity. From a potential liability standpoint, it's important during this period for you to be especially careful regarding your professional relationship with the client. You don't have to act as if you are a medical professional, but you should make your concerns known to appropriate individuals. You also should exercise care when making and acting on recommendations.

This also is the time to recommend that the individual make arrangements for someone(s) to have authority to legally represent the individual if he or she becomes completely incompetent. Such arrangements should have been made sooner, but later is likely not a viable option, so now is the right time. It will be important to include family and/or trusted friends in the process, so you are not seen as trying to take advantage of the client, and so you can get the support you need to help the client. We will look at some of the legal options in a later section.

Severe Cognitive Impairment

Cognitive impairment, related to progressive dementia, can move through five stages (Taylor & Ballentine, 2017):

1. No impairment
2. Questionable impairment
3. Mild impairment
4. Moderate impairment
5. Severe impairment

At the severe impairment stage, the individual no longer is able to function independently. In a situation where the onset of mental incapacity is gradual, neither the individual, nor family members, especially those who do not live nearby, may be fully aware of the progression. As you meet with the client, you might be able to notice what the family has not and proceed accordingly. Individuals severely impacted by dementia/cognitive impairment may experience loss of motor skills and may lose the ability to speak. During this stage the brain may seem to lose its connection with the body. The individual will need help with all manner of normal functioning (Dementia.org, 2017).

Assessment for severe cognitive impairment may include the following categories (FCA, 2004):

- Personal care: bathing, eating, dressing, toileting, grooming
- Household care: cooking, cleaning, laundry, shopping, finances
- Health care: medication management, physician’s appointments, physical therapy
- Emotional care: companionship, meaningful activities, conversation
- Supervision: oversight for safety at home and to prevent wandering

Older people tend to exhibit greater nervousness and confusion as part of the aging process. Adults suffering from severe cognitive impairment will exhibit far greater amounts of anxiety and confusion. Again, this may be reason enough to take some preventative measures regarding the client. When a client reaches the severe stage, it is unlikely you will be able to continue working with him or her. Often, they will have been moved into an extended care facility, but even when they remain at home, their ability to function will be significantly compromised.

Documents to File

Several types of documents that provide advance directives for medical and other personnel can be applied. The exact forms to use will vary by territory, as will the names used to describe them. However, many territories allow for one or more varieties of these documents to be applied in appropriate situations.

Advance (care) directive. A broad category of documents identifying the individual's desires for ongoing treatment when incapacitated.

Durable (enduring) power of attorney (health care proxy). Unlike a regular power of attorney (POA), which ceases when the principal becomes incapacitated, a durable or springing POA can function as a health care proxy in the event of incapacity. This will authorize a trusted individual to make health care decisions on the individual's behalf, based on previously stated desires. A durable power can begin when the individual is at normal capacity and continue through incapacity.

Health care/medical power of attorney. A medical POA grants specific authority for a representative to take control over health care decisions in the event the principal becomes incapacitated.

Springing power of attorney (conditional). A springing or conditional power differs from a durable power in when it begins. A springing power is not in effect until a specific event occurs. For our purposes, the event is when the principal becomes disabled or mentally incompetent. The power *springs into effect* when the principal becomes incapacitated.

Living will. A living will provides direction to attending physicians regarding the level and degree of care the individual desires. This usually comes into play when the end of life seems imminent. A person's living will might state that, in the event of extreme, life-threatening, incapacity, medical personnel are not allowed to implement *extraordinary* or *heroic* measures to extend the person's life. A living will is a type of advance directive.

Revocable living trust. Where it is allowed, a revocable living trust in which the principal is the trustee, can provide a way to oversee legal and financial matters related to a person's assets. However, this will only be true if a successor trustee is named, who will take over when the principal is incapacitated.

In addition to the health care related forms, an individual should make arrangements for legal and financial representation as needed. This can be done using a durable POA to give authority to an individual to make legal and/or financial decisions on behalf of the principal. As the financial planner, you may come in contact and need to work with such an individual. If you do, be sure to validate their authority prior to divulging private information or taking any action based on the representative's instructions.
One of the advantages to drafting and filing a legally binding document, such as we have been exploring, is it can allow a significant person who is not a spouse to act on behalf of the principal. A spouse often is granted at least a limited right to act on behalf of the other spouse. Most territories limit the rights of unmarried partners in this area. An advance directive, durable POA, or similar can reinstate those rights.

Part of planning for incapacity should include ensuring a person's will is updated, valid in the territory, and accurately expresses desires for estate distribution. One of the first steps for this is writing down detailed instructions related to what the individual wants to have happen in the event of incapacity. The individual also should have a conversation with a trusted associate (e.g., family member, friend, advisor) to convey those desires. When coupled with appropriate legally recognized forms (e.g., durable POA), the person's desires are much more likely to be implemented. Authorized individuals should have access to important papers (e.g., insurance policies, financial and medical contacts, financial/bank account information, last will and testament, health care directives, etc.), and family members should be notified of the individuals' decision to authorize the representative.

This chapter provided an overview of how to make arrangements for potential incapacity. It's a crucial area to address, and unfortunately, one that many people (and advisors) tend to overlook. In the next chapter, we will look at some broader estate planning strategies the client can implement.

Example 1		
Question		*Many people struggle to plan for potential incapacity. One simple reason being, they never consider that it could happen to them. As their financial planner, you can provide a valuable service by educating clients about the potential incapacity and what they can do to prepare in the event it impacts them. As a financial planner, you cannot do an analysis, but when working with a client, you may notice some signs of MCI. Which of the following is least likely a symptom of mild cognitive impairment?*
	A.	Losing a train of thought or conversation thread.
	B.	Becoming more impulsive or showing increasingly poor judgment.
	C.	Postponing financial decision-making or planning steps to accomplish a goal.
	D.	Forgetting important events such as appointments or social engagements.
Correct Answer		**C.**
Explanation		This can be normal behavioral trait in people who do not have inclination to understand finance and have exposure to financial decisions-making process.
Distractor #1	**A.**	Failing to respond in a conversation as if sudden drain of recent memory has happened is one of the symptoms of MCI.
Distractor #2	**B.**	Feelings of impulse to get around simple things and showing poor judgment in a sustained manner in normal events is a sign of MCI.
Distractor #3	**D.**	Forgetting important dates, such as failing to recall birth dates of self, spouse, important events, social engagements and schedules is a sign of MCI.

Discussion Questions

1. What is incapacity and how can it impact an individual?
2. As a financial planner, what should you do when you suspect a client is exhibiting symptoms of mild cognitive impairment?
3. What are some of the forms that can be used to address issues of cognitive impairment and how might they be applied?

Chapter Review

1. What is incapacity and how may it impact an individual?
2. What are core elements of a medical workup for mild cognitive impairment (MCI)?
3. What are some key symptoms of MCI?
4. As a financial planner, what can you do if you recognize that a client is experiencing MCI?
5. What are the stages through which cognitive impairment can pass?
6. What are some of the advance directives (legal documents) that can be used to prepare for the possibility of incapacity?
7. Why is a regular POA not a good choice when a person becomes incapacitated?

Chapter 6: Estate Planning Strategies

Learning Outcomes

Upon completion of this chapter, the student will be able to:

6–1 Assess specific needs of beneficiaries
6-2 Develop estate planning strategies
6-3 Evaluate advantages and disadvantages of estate planning strategies

Introduction

The primary emphasis of financial planning is to develop strategies that help clients achieve life goals. Within the area of estate planning, the emphasis is on developing strategies that help the client achieve end-of-life goals. These goals may begin long before life ends by giving gifts, providing endowments, adjusting business arrangements, and so forth. End-of-life arrangements typically focus on distributing the person's estate in the most efficient, effective manner, and in accordance with stated goals. In all cases, the needs of beneficiaries (i.e., survivors who will inherit assets) should be paramount in the planning.

Common Concerns

Before we look at some specific scenarios, we need to consider some concerns that are consistent for estate planning generally. A financial planner should be ready to address six estate planning concerns (Leimberg, Satinsky, Doyle, & Jackson, 2012, pp. 155, 156):

- Lack of liquidity
    - Need to have sufficient cash to meet settlement costs, taxes, and other final expenses
- Improper disposition of assets
    - Preventing assets from going to the wrong people, at the wrong time, or in the wrong manner
- Inadequate income or capital
    - Need to provide for ongoing retirement expenses, special needs (see below), the client's disability or incapacity, and family living expenses after the individual's death
- Asset values destabilized and not maximized
    - Desire to keep business valuations as high as possible and assets distributed in ways that do not unnecessarily reduce their value
- Excessive taxes and transfer/distribution costs
    - Keep final expenses and taxes to a minimum
- Special needs
    - Provide ongoing care for a spouse who is not financially capable, children or parents who are not able to care for themselves (e.g., mental or physical disability), and support for exceptionally gifted children

Spouse, Partner, Ex-Spouse

It's likely that a current spouse or partner immediately comes to mind when planning. Financial planners also should understand that, sometimes, the needs of an ex-spouse and children may represent a desired planning focus.

Spouse

Depending on the territory, providing for the needs of a spouse may be written into the law, or perhaps not. This is not an area to be left to chance. Though some spouses may want to disinherit the other, this is not something most territories will allow (even if the attempt is made).

It's often possible the surviving spouse will remarry, but that possibility should not be a planning focus. Instead, planner and client should consider what the surviving spouse (of either gender) will need to move forward with life as a single individual. This may include caring for dependent children (and/or parents) as well as themselves. It may include the decision to continue or close a family owned business. It also can move into the area of personal well-being and address a support network, ongoing health care, sufficient income, support during a transition period, and more.

A surviving spouse will enter a period of grieving. The exact parameters of grief and coping methods are personal and individual. That said, most people share some degree of similar experiences during this period. Grief—especially when it is extreme, as can be the case when a spouse dies—has an impact on how the surviving spouse thinks and feels. Mental clarity often is diminished for a time, and it can become difficult even to get through each day.

The surviving spouse may experience many emotions that swirl around and can resurface multiple times. Some of these may include feeling (NEFE, 2017):

Angry	Annoyed	Anxious	Bitter
Crushed	Depressed	Despairing	Doubtful
Fearful	Guilty	Helpless	Hopeless
Nervous	Outraged	Panicked	Perplexed
Rejected	Scared	Shocked	Terrified

This is not the time to make any major life decisions, which supports the rationale for making enough preparations ahead of time so the surviving spouse can rely on those arrangements rather than having to make all decisions in the moment. At the most basic level, preparations can include funeral and burial planning, providing an updated list of trusted advisors (e.g., legal, financial, accountants, spiritual, etc.) and making a list of things like online account access and location of documents.

It may be helpful for the financial planner to provide guidance to the surviving spouse to help him or her clarify areas of concern, including those things about which he or she has questions. As an example of such a checklist, consider the following (NEFE, 2017):

Figure 3: Life Events Questions

What don't you understand?
What don't you know?
What have you assumed (but not confirmed)?
What would help you feel more comfortable?
What would ease your fears?
What specifically do you want others in your life to do to support you?

Financially, planning can include life insurance policy documentation, including beneficiary arrangements, insurer contact information, policy numbers, and the like (to file claims and possibly to cancel policies). The surviving spouse will need to know which other insurance policies should be continued and paid, and which should be terminated. The same is true with credit accounts, such as personal loans, mortgages, credit card accounts, car loans, etc. The spouse will need to know about all investment and banking accounts, and how to access them—remembering that territorial succession rules and legal beneficiary arrangements may impact the ability to have access to these accounts. This also will be true with ongoing retirement benefits and any other social security benefits. Some bills will have to be paid immediately, and this information should be readily available to the surviving spouse.

The surviving spouse will have to obtain documentation that the decedent has died. This may be needed to present to any number of institutions, so multiple copies of such certificates of death probably will be necessary. Requirements in this area vary by territory and by institution. In some cases, papers must be in legal form and signed by appropriate authorities. Other situations may not have such formal requirements, but it's worth preparing for the potential need.

It may be necessary for the surviving spouse to retitle the family house and perhaps a continuing mortgage in his or her name. The same can be true for other assets, such as a car, land, and financial accounts. Having a trusted lawyer and financial advisor on board will be helpful in this process.

The surviving spouse will have to locate and submit the decedent's will for processing (e.g., probate). The process will require a legal representative, and choosing one ahead of time will be helpful for the spouse. The finalization process may take an extended period of time, so providing for adequate liquidity (cash flow) during the period will be necessary. Often, one or more life insurance policies can provide for this need.

A financial planner likely will not be able to address the surviving spouse's needs for community, but this should be considered as part of the estate planning process. The spouses should discuss (ahead of time) who can be trusted and to whom the survivor can turn for comfort, guidance, support, and general help. Having a strong support network (even if only a person or two) can be a big help to the remaining spouse. The spouse will have to contact family, friends, and other key individuals with the news of the death, and it can be comforting to have a trusted friend available to help.

There are a few things that should *not* be done immediately following the death of a spouse. These include selling the house or other property and giving away cash or other assets (even to children). The surviving spouse should be careful not to make any major financial, legal, or lifestyle change for a period of time (e.g., at least six months to one year); not succumbing to pressure tactics by anyone who wants to attach available assets. Sometimes this can be done by an otherwise trusted individual, so extra care may be needed (another good reason to have a strong support network, including legal and financial advisors). The categories listed in the following table can provide guidance for the surviving spouse as he or she considers some needs and a potential support network (NEFE, 2017):

Figure 4: Surviving Spouse Support Network

Type of Support/Advisor	I need this help now	I will need this help in the future	I do not need this support
Emergency recovery (food, shelter)			
Attorney/legal advice			
Tax expert			
Doctor/general			
Doctor/specialist			
Nurse/long-term care			
Hospice/end-of-life care			
Physical therapy			
Rehabilitation therapy			
Psychiatrist/psychologist/counselor			
Support group			
Insurance agent			
Financial planner/advisor			
Investment advisor			
Career counselor			
Relationship counselor			
Mediator			
Child care			
Elder care			
Pet care/boarding			
Mortgage broker			
Real estate agent			
Apartment finder			
Handyman/home repairs/contractor			
Car mechanic			
Electrician			

Plumber			
Other:			

Unmarried Partner

Most, if not all, of the considerations for a surviving spouse apply to a surviving unmarried partner. However, an unmarried domestic partner may not have the same rights or support network as a surviving spouse. In general, an unmarried partner will require at least as much, if not more, specific estate planning clarity and documentation as does a surviving spouse. The decedent's instructions in a will must specify the partner (when desired). The same is true for beneficiary arrangements on life insurance policies, continuing retirement income plans, and similar. Remember, not all territories acknowledge or accept the legality of unmarried partnership arrangements. As a result, some spousal-type planning will not work in these territories. For example, it's possible that, even though a decedent's will identifies the partner as a legal beneficiary, territorial succession rules may invalidate that designation.

Unmarried Partner not Recognized Example. Maria's partner recently died. Prior to his death, he assured Maria she would be taken care of through the terms of his will. Unfortunately, as Maria works through the probate process, her situation is not looking good. The territory in which she lives follows a strict forced heirship scheme and does not recognize unmarried partners as a legal entity. As a result, even though Maria's partner made arrangements for her in his will, the probate court doesn't look as if it will honor those arrangements. Instead, the court is favoring distribution to the decedent's children from a prior marriage. Essentially, the children will divide their father's estate in its entirety. As a result, even though the total estate is valued at $2 million, Maria will receive nothing.

If Maria's partner and their financial planner had been able to establish and fund a trust for her benefit, named her as beneficiary of a life insurance policy on his life, or provide *inter vivos* gifts to her, Maria would not have her current financial concerns.

Sometimes this can be overcome by other contractual arrangements (e.g., life insurance beneficiary nomination). Where territorial laws allow all or some portion of a decedent's estate to pass to a surviving spouse tax-free, a surviving partner is unlikely to receive the same benefit. As in other ways, adequate life insurance with appropriate beneficiary designations can be helpful to provide the funding necessary to pay taxes and other expenses.

A financial planner who works with an unmarried couple should be aware of legalities in the territory and advise the partners accordingly. Be sure to make arrangements for things such as durable powers of attorney (or similar). Without appropriate legal documentation, the partner may not be allowed to participate in end-of-life care for the other partner. He or she may not even be allowed to be by the side of the dying partner in the hospital/medical facility.

It also may be a good idea to suggest the partners retitle assets (e.g., bank and investment accounts, real property/real estate, etc.) so they are jointly owned with appropriate rights of survivorship, as these will pass by law to the surviving partner. Where recognized, a living or testamentary trust may be a good vehicle for assets to pass to the partner. As is often the case, competent legal counsel will be helpful.

Emotionally, an unmarried partner almost certainly will experience the same feelings, and have the same thoughts and concerns, as a married spouse. A well-functioning support network may be even more important to a surviving partner than it is for a surviving spouse, because of different legal practices and social and cultural mores.

Ex-Spouse

Some ex-spouses, perhaps many, do not part amicably, and they may not want anything further to do with the ex. Other times, an ex-spouse can remarry, and the new marriage can make any relationship with the other party undesirable or impossible. However, there can be times when spouses have gone separate ways but remain friendly. Perhaps they share children or grandchildren. Maybe they no longer are together, but neither one has entered into a relationship with another person. It may be possible that applicable laws (especially regarding children) mandate a degree of provision and/or accommodation between the two. Whatever the situation, a financial planner may be placed in a situation where he or she must do estate planning with a focus on the ex-spouse.

Many of the legal and financial considerations applicable to unmarried partners will apply to ex-spouses. Laws in the territory are likely to have terminated all legal and financial arrangements as of the severing of the marital agreement. As a result, if the ex-spouses want particular estate planning provisions, they will need to specifically identify these and make appropriate legal documentation (starting with an updated will).

One situation that has perhaps a greater likelihood of occurring is the desire, need, or requirement to provide for children from the former marriage. These children may or may not be included in any forced heirship regimes. If they are not, they may be in danger of being disinherited. Most times, this is not the desire of the ex-spouses, nor is it in the children's best interest. As is true for the ex-spouse, appropriate documentation in an applicable will is an important place to begin. Both spouses should include the children, often by name (rather than generically by class), in their respective wills. Care will be needed to provide for other children, including those from any current marriage. Where possible, the parents may wish to structure a trust to provide for the children. This is another scenario where proper beneficiary designations, including naming an administrator/guardian for the children, can solve many problems. Legal determinations from divorce proceedings may require a specific irrevocable beneficiary designation or similar for the benefit of the children. This will have to be included in estate planning considerations. Depending on the relationship between the ex-spouses, multiple meetings, perhaps both separately and together, may be required to make the necessary arrangements.

These types of beneficiary arrangements can become problematic when the children reach the age of majority. When initiated, it may have been appropriate to name the children's parent(s) irrevocably as guardian or administrator for the children. After they reach the age of majority, this arrangement no longer may be desirable. However, when the beneficiary designation that included the ex-spouse was made irrevocable (especially when mandated by the court), it cannot be changed without consent of the ex-spouse, and sometimes, the court. As the financial planner, you cannot directly intervene, but you should be aware of the potential difficulty.

Another option for distributing assets to children or grandchildren from a prior or current marriage is to make a lifetime gift.

Lifetime (*Inter Vivos*) Gifts

Gifts are not only used to provide for children or grandchildren, they can be made to benefit spouses, partners, parents, friends, business associates, charitable organizations, and more. An individual can make a lifetime gift of any owned assets in almost any way he or she wishes. There may be laws in the territory that place limits on gifting, but normally, especially when the gifts are not particularly large, the options are close to limitless. After a gift reaches a certain amount of money or value, all or part of that gift may be taxable, depending on the individual or organization to whom it is given. That said, and taxability aside, the gift still can be given however and whenever an individual desires to do so.

The simplest method of making a gift is to give it outright. That is, shift beneficial and legal ownership of an asset, property, or cash from the donor to the donee/recipient. It's a straightforward approach, and if monetary amounts are within legislative limits, it is unlikely to be a taxable event for either party. In addition to possible tax issues, perhaps the biggest potential downside to making a gift is loss of control for the donor. To be a true gift, the donor has to relinquish control of the asset. He or she sometimes may retain an interest in the asset (e.g., income for a period of time), but overall, when a person gives away an asset, he or she gives away all rights associated with the asset. If the donor is prepared to part company with an asset, this presents no problem. However, it's a question that must be asked and a decision made prior to making any gift.

One of the greatest advantages of giving a lifetime gift is the satisfaction that comes from seeing the recipient enjoy the asset. Whether the gift is a small monetary amount or a parcel of real property, a significant investment portfolio or a single stock, when it is given during the lifetime of the donor, he or she will have the opportunity to see the result of giving the gift. Consider a donor who gifts a sizeable sum to a favorite charitable organization. The organization will then be able to apply the gift to help achieve its mission/purpose. The donor will have the opportunity to see this in action and receive satisfaction from knowing he or she helped accomplish the organization's work and purpose. Perhaps the donor is a grandparent wanting to ensure a grandchild has the funds necessary to attend university without having to pay their own way. The grandparent can pay tuition and related expenses, knowing the grandchild will be moving forward toward a chosen life or career path. A father or mother can turn over a family business to one or more children and help them manage and grow the business. A parent can give a child financial support to get help care for a new baby. The gifting possibilities are many and the frequent result is great satisfaction.

Taxation

Lifetime gifts also may enable the donor to reduce the size of his or her estate, thereby reducing related taxes and fees. Gifts usually are more private than testamentary transfers, too (since probate is public information). Giving a gift of an appreciating asset can remove future growth from the donor's estate. The gift may have current tax implications (e.g., gift or income), but once given, the donor's estate will not be liable for any increase in value associated with the gift. The donee will deal with the gain, not the donor. If a gift is potentially taxable, a gift tax exemption may be applicable that will reduce current taxes. Using the exemption, especially with systems using a unified tax

scheme, may result in a greater amount of tax being due on testamentary transfers, but current impact will be reduced.
Taxation presents a possible dilemma. Valuing a lifetime or testamentary transfer is reasonably straightforward. The recognized or appraised valuation at the time of transfer is the value. What is in question is the gift's *basis*. Tax basis is subtracted from the current valuation to determine possible taxation. For example, a $100,000 gift with a basis of $25,000 will potentially have taxation based on the remaining $75,000 (i.e., $100,000 – $25,0000 = $75,000). The question arises as to what will be considered the asset's basis. There are two primary options. The first is for the donee to take over the donor's basis. This means, with the previous example, the recipient's basis will be $25,000, the same as the donor's. Any taxation will use $25,000 as a starting point. Depending on the territory, there may be a second option. Testamentary transfers may receive a *step-up* in basis. This means that the asset will receive a new basis, and it will be the value at the time of transfer. With our example, instead of a $25,000 basis, a testamentary transfer will have a new basis of $100,000. Now, any taxation will use $100,000 as the starting point rather than $25,000. This is not a consideration to be taken lightly. The monetary amounts do not tell the whole story, but they can play a significant part in the decision of whether to give a lifetime gift or wait and make a testamentary transfer. The client will have to make the decision, based in part on the financial planner (or accountant) evaluating the implications of both options.

Special Needs
Sometimes, a situation will present itself that almost requires a lifetime gift to be made. One such situation is when a dependent—child or parent—has or develops a special need. The nature of special needs can be mental, emotional, physical, or a combination. Regardless of the nature or cause, a dependent with a special need almost always requires specific care and additional funding. The care may be provided by family or professionals. The funding, at least in some cases, may be considered a gift. When the authorities deem the funds to be a gift, the usual tax considerations may apply, or an exemption/exclusion may apply.

One option of providing funds for current and future care is to establish a special needs trust or its equivalent. A special needs trust, as the name implies, is a vehicle to hold cash or other assets that will be used to pay for necessary care, housing, and other expenses, and provide spending money for the beneficiary. It's possible, by placing assets in the trust, the beneficiary will retain the ability to receive additional government-provided aid that might not be available if the funds were given directly to the individual. Typically, a trustee will oversee how trust assets are distributed, including paying for caregivers, medical needs, housing, education, and other expenses. Government funds also may be available to provide a portion of the necessary financial support. The financial planner and family should use care in establishing the trust (or other) vehicle to ensure it is done in such a way as to receive all potential tax and other benefits and contains no provisions that may stand in the way of accomplishing its purpose.

Dependent children are the most common special needs beneficiaries, but one or more parents may have a similar need, and may benefit from the same type of solution.

Children and Grandchildren

Previously, we looked at providing for children from a prior marriage. Doing so may present challenges that differ from providing for children from the current marriage. Regardless of whether the children are from a former or current marriage/partnership, are adopted or step-children, parents normally want to ensure provision is made for them. This may be done via lifetime gifts, testamentary transfers, or (often) both. When a territory holds to a mandatory succession (i.e., forced heirship) regime, the state may require a specific allocation of estate assets to be distributed to children (especially those from the current marriage). Lifetime gifts can be used to provide an inheritance substitute for one or more children. It may be that children from a prior relationship are in danger of being disinherited by mandatory inheritance rules, and the parent wants to ensure this does not happen. It's also possible that a parent may want to provide a larger percentage share of assets to one or more children than to others. For example, one child may have great personal wealth while another is impoverished (for whatever reason). The parent may want to bias asset distribution in favor of the impoverished child. One or more lifetime gifts may facilitate this desire.

Exceptionally Gifted Children

Providing for children who are exceptionally gifted may not automatically come to mind when considering estate planning strategies. However, these children have special needs of a different type than previously explored. Exceptionally or highly gifted children can include those who have very high intelligence, prodigious abilities in music or mathematics, or exhibit great abilities in other areas. Exceptionally gifted children may be highly gifted in one area but may seem much less developed in other areas. This can be exhibited in their school performance, social interaction, relationships at home, and similar. The specific indicators are not overly applicable to the current observation. What is important, however, is that these children can easily be underserved without special attention. It's unlikely their giftedness will go away, but without appropriate support, it may not develop into what it might with proper nurture. The reason for highlighting this group is that they, like special needs dependents, will benefit from additional care. One of the first things that comes to mind for estate planning purposes is for the parents to establish a fund or trust to provide additional education and support that will help these children grow into exceptional adults. It may be that regular public schooling will not suffice. Instead, the exceptionally gifted child might benefit from attending an educational institution that can provide special attention. This almost certainly will require additional funding and is something to be addressed during the estate planning process. It's also possible that a specially trained and knowledgeable guardian/mentor should be a part of the instructions parents provide in the event of their death.

Grandchildren

All of the considerations in the preceding paragraph may be applicable to grandchildren as well. Most grandparents who have the ability to do so, want to provide for their grandchildren in addition to their children. Several territories levy an additional tax when assets are transferred from the decedent to a grandchild, skipping a child. In this situation, the grandchild may be known as a *skip person* or *direct skip*. A skip person is a beneficiary more than one generation away from the decedent (e.g., a grandchild in relation to a grandparent). Assuming there is no exemption from paying a special generation-skipping transfer tax, it may be possible to reduce or eliminate potential taxation using a generation-skipping trust, or similar. A generation-skipping trust, in simplest form, divides title to the asset from usufruct. Usufruct goes to the immediate child of the decedent while the title is held, in trust, for the benefit of a grandchild. When the child eventually dies, the usufruct will merge with the actual title for benefit of the grandchild. This effectively avoids negative taxation consequences of skipping generations (Ernst and Young Global, 2017).

Intrafamily Transfers

Wanting assets to remain in the family often is a common goal. The same is true for parents wanting to help children, especially in a financial way. We have looked at the potential to make lifetime gifts to family members (as well as to others). Technically, when a parent, grandparent, or other close relative makes a gift to a family member, it can be called an intrafamily transfer. This means that the gift, or transfer, is being made within the family rather than extending to a charitable organization or nonfamily beneficiary. When a gift is made, whether it goes to a family or nonfamily beneficiary, it will be subject to gift and perhaps inheritance rules in the territory. This means that taxes, re-registration requirements, impact of ownership interests retained by the donor, and any other related rules and regulations apply. It also is possible that special exemption limits can be applied to transfers from one family member to another, especially when the gift is made to a spouse or children.

Another method of making an intrafamily transfer is through use of a loan. Each territory has its own rules for this, but we can identify some commonalities. First, the intent will be to differentiate the loan from a gift. If the donor wants to give a gift, no loan is needed—he or she can just make the gift. However, because gifts fit into a category that may create a taxable event, and use at least a portion of any exclusion amounts, sometimes the parent may want to avoid having a transfer classified as a gift, but still want to make the transfer to children or other family. As a result, a loan may present a workable solution.

To be a loan, a financial transfer must have a legally recognized agreement, a stated rate of interest (which, in some cases in certain territories, may be 0%), and a repayment period with minimum required payment amounts. In other words, the requirements for an intrafamily loan basically are the same as for a non-intrafamily loan. Assuming the required agreements will be in place, an intrafamily loan can be a little different from a nonfamily/commercial loan. For one, the interest rate charged can be quite a bit lower. The government may have regulations regarding how low the rate can be, but it's almost always lower than typically available on the open market. The repayment period also can be extended beyond what normally would be the case, and minimum required payments may be lower, too. Additionally, it should be noted that repayment amounts stay in the family (e.g., from the child to the parent), and can be used to increase cash flow or for whatever purpose the parent wants to make of it.

When an intrafamily loan is used to transfer a family business, house, farm, or other real property from parent to child, it has the additional benefit of keeping the asset in the family. Often, this is the parent's intent. A word of caution around valuing the business/property: It has to be realistic in the current marketplace. In other words, the parent cannot simply state that a business actually valued at $1 million will have an intrafamily loan value of $100,000. The difference between the two values ($900,000) will be deemed a gift and treated accordingly. On the plus side, an intrafamily transfer/loan effectively freezes the asset's value as of the execution of the transfer. So, if a transferred business is valued at $1 million and grows over time to be worth $10 million, the valuation to the parent for estate-tax-related purposes remains $1 million. The child will have to deal with the increase in value, but the parent will not. Application of this principle will vary by territory, and the transaction must follow applicable laws, but it can be an effective tool to keep assets in a family and, at the same time, reduce the estate tax burden on a parent.

Perhaps the biggest potential pitfall of an intrafamily loan is allowing the loan to become a gift. A parent may make a loan to a child and then forget about it. When this happens, the *loan* remains part of the parent's estate and can be taxable. A child may receive a loan, sign a repayment agreement, but not honor the agreement. If the parent does not enforce the repayment requirement, the loan will be considered a gift and treated accordingly.

Intrafamily Loan Example. Phillip and Faye started their bakery 40 years ago and have built it into a thriving business. The couple is tired of working the long hours required to run the bakery and would like to transfer business ownership to their three children. The children have been working in the bakery for several years and would like to keep it going, but they do not have the money to pay the purchase price. When Phillip and Faye spoke about this to their financial planner, she suggested an intrafamily loan. Here's how it would work, she said. Phillip and Faye could work with a lawyer to draw up papers to transfer the business to the children. As payment, they could arrange a loan with a nominal down payment and an interest rate at the very low end of current rates. The children would repay the loan over a 10-year period by making payments each month. Profits from the bakery could be used to help with the payments. The payments, along with some ongoing revenue from the bakery, would provide an income stream to Phillip and Faye. They would also be able to help the children manage the bakery during the transition period and regular customers would still see them at the bakery. The children agreed to the plan and now the bakery is under new ownership. Phillip and Faye are happy to keep the bakery in the family and the children are pleased to be able to make the transition work.

Small *de minimis* loans (or gifts) may not even register for potential government (tax) action. However, when the amount is large enough—e.g., to purchase a home, buy a business, or similar—the government is much more likely to take notice. This is why, in most circumstances, the loan must comply with normal loan requirements (e.g., written agreement, etc.) and follow an agreed-upon repayment schedule. To be sure, some territories do not require an intrafamily loan to follow the same guidelines as a commercial bank, but many do. If the goal is not to make a gift, applicable regulations must be followed (experienced professional guidance is recommended). Care also should be exercised when considering the possibility that a married child gets divorced from his or her spouse. In the divorce decree, the property may be granted to the ex-spouse, and this almost never is what the parent desires. As a result, legal documentation to prevent this should be included in the original papers.

Disclaiming an Inheritance

Most people do not think much about refusing to accept an inheritance—they're happy to receive what they have been given. Sometimes, though, an inheritance is not the gift it was intended to be. Perhaps the heir already has a sufficient amount of assets and does not wish to increase his or her personal fortune. Regardless of the reason, there are times when an heir/beneficiary does not want to accept an inheritance. When this is the situation, it may be possible for the individual to *disclaim* or renounce the inheritance. Disclaiming an inheritance is a formal (and legal) rejection of the property. Why would someone want to reject an inheritance? There may be many reasons, two of which are associated debt and extreme inconvenience.

When a person inherits an asset, often they also inherit any debt associated with that asset. Sometimes the debt can be quite large; large enough that the positive value of the asset is overshadowed by the debt. As a result, the beneficiary may decide not to accept the asset and thereby avoid inheriting the debt. In many situations, debts can legally be collected beyond territorial boundaries. For example, a debt from South Korea may be due and payable by an heir in Canada. There usually is a limited time during which an inheritance may be disclaimed (e.g., three months), and specific legal requirements to implement the disclaimer. As a result, it's important to act quickly. An alternative to disclaiming an inheritance is for the potential heir to request an inventory followed by an official liquidation of assets. Debts can be paid from the liquidated amounts, with any excess distributed to heirs.

A second reason used to disclaim an inheritance is inconvenience. This is most likely to occur in cross-border situations, but also may be relevant within a territory. A potential heir may live on one side of the territory, and the business he or she has inherited is on the other side. Perhaps the real property (e.g., house, farm, etc.) is so far from the heir that he or she cannot manage it. Perhaps the heir has a life and job in a city that will not allow them to easily interact with the inherited property. Whatever the reason, the potential heir does not want to assume ownership of the property. He or she can disclaim the inheritance in the same way as when excessive debt is a consideration.

Disclaiming Inheritance of Polluted Land. Terri's father recently died, leaving Terri with a parcel of land. The land looked as if it could be developed for commercial use, so Terri began to look into the potential to see whether she could develop the land, sell it, and use the proceeds to supplement her retirement portfolio. Within a few days Terri received the report and learned that the land had been cited as being environmentally polluted by previous mining activities. Chemicals used in the mines had leached into the land's water supply and were also being deposited on the land itself. The environmental report indicated that reclaiming the land and cleaning up the pollution would cost the owner at least $10 million. Additional findings of pollution would increase the costs. Terri did a quick analysis to determine that, coupled with the cost of development, cleaning up the land would be cost prohibitive and would not allow her to have a viable return on any land development. Terri sought legal counsel and elected to disclaim her father's inheritance, because the costs would outweigh any positive value she would receive.

Disclaiming an asset usually has greater tax-related benefits than receiving the asset and then giving it away (even to another potential heir). Receipt of an inherited asset often is a taxable event, and the recipient will be responsible for paying associated taxes. Then, when the new owner decides to gift or sell the asset, he or she may be faced with another taxable event. These taxes may be investment or gift related, or perhaps added to income and taxed. Regardless of how the taxes are assessed, the new owner may have to pay a greater amount of taxes than if he or she disclaimed the inheritance and allowed it to pass directly to another heir.

A final consideration in this area involves a warning. It’s possible that family members living in the area of the inheritance may encourage the potential heir, living some distance from the inheritance, to disclaim it, waiving any rights to inherit. This may be done with good intent, but perhaps not. The nearby family simply may want to inherit the asset(s) for themselves. Getting the primary heir to waive inheritance rights opens the door for a nearby relative to move in and claim the asset. This may occur in cross-border situations more than when all parties live in the same territory, but it does happen. Prior to disclaiming, especially in a cross-border scenario, the heir should conduct a reasonable investigation as to the status of inherited assets and associated debts. The investigation may uncover less-than-honorable intent from the third party (Hayes, 2017).

Example 1		
Question		The primary emphasis of financial planning is to develop strategies that help clients achieve life goals. Within the area of estate planning, the emphasis is on developing strategies that help the client achieve end-of-life goals. Wanting assets to remain in the family often is a common goal. The same is true for parents wanting to help children, especially in a financial way. Gifts are sometimes used provide for children or grandchildren. When a gift is made, whether it goes to a family or nonfamily beneficiary, it will be subject to gift and perhaps inheritance rules in the territory. Another method of making an intrafamily transfer is through use of a loan. Each territory has its own rules for this, but we can identify some commonalities. Which of the following statements regarding intrafamily loans is most likley true?
	A.	A loan fits into a category that may create a taxable event.
	B.	An intrafamily loan cannot become a gift.
	C.	An advantage of an intrafamily loan is that the parent cannot simply state that a business actually valued at $1 million will have an intrafamily loan value of $100,000.
	D.	To be a loan, a financial transfer must have a legally recognized agreement, a stated rate of interest (which, in some cases in certain territories, may be 0%), and a repayment period with minimum required payment amounts.
Correct Answer		**D.**
Explanation		To be a loan, a financial transfer must have a legally recognized agreement, a stated rate of interest (which, in some cases in certain territories, may be 0%), and a repayment period with minimum required payment amounts.
Distractor #1	**A.**	Because gifts fit into a category that may create a taxable event, and use at least a portion of any exclusion amounts, sometimes the parent may want to avoid having a transfer classified as a gift, but still want to make the transfer to children or other family. As a result, a loan may present a workable solution.

Distractor #2	**B.**	Perhaps the biggest potential pitfall of an intrafamily loan is allowing the loan to become a gift. A parent may make a loan to a child and then forget about it. When this happens, the loan remains part of the parent's estate and can be taxable. A child may receive a loan, sign a repayment agreement, but not honor the agreement. If the parent does not enforce the repayment requirement, the loan will be considered a gift and treated accordingly.
Distractor #3	**C.**	The parent cannot simply state that a business actually valued at $1 million will have an intrafamily loan value of $100,000. The difference between the two values ($900,000) will be deemed a gift and treated accordingly. On the plus side, an intrafamily transfer/loan effectively freezes the asset's value as of the execution of the transfer. So, if a transferred business is valued at $1 million and grows over time to be worth $10 million, the valuation to the parent for estate-tax-related purposes remains $1 million. The child will have to deal with the increase in value, but the parent will not.

Discussion Questions

1. Overall, how do common and civil law territories differ regarding succession practices and estate planning?
2. Is the probate process generally positive, negative or a combination of the two?
3. How is a living will different from a testamentary will (i.e., last will and testament)?
4. What are some of the different property ownership (titling) arrangements and how may they impact estate distribution.
5. How may a forced heirship regime impact a decedent's estate plan?
6. How and why would a special needs trust (or similar tool) be applicable in an estate planning scenario?
7. How does an intrafamily loan differ from a nonloan intrafamily transfer? When would you suggest one over the other?
8. What benefit is there to disclaiming an inheritance and why would a potential heir go through the disclaiming process?

Chapter Review

1. What are six estate planning concerns a financial planner should be ready to address?
2. What impact can grief have on a surviving spouse's ability to think and make decisions?
3. What duties or responsibilities may a surviving spouse have as part of estate settlement?
4. What are some decisions that should not be made immediately following death of a spouse?
5. What is the biggest potential difficulty an unmarried domestic partner may face when their partner dies and what can be done to address these concerns?
6. What is a situation in which ex-spouses may need to work together to do estate planning?
7. What must be done for a gift to be considered a true gift?
8. What is the function of a special needs trust and, where allowed, how may it be used?
9. What must be true for an intrafamily loan to be considered a legitimate loan?
10. What are some of the differences between an intrafamily loan and a commercial loan, and how may this benefit a family?
11. What are two reasons an heir might want to disclaim an inheritance?

Summary

In this course we have explored much of the terminology related to estate planning. This included terminology that is applicable to bequests and testamentary transfers, along with lifetime, *inter vivos* gifts. We looked at common goals related to an individual who does estate planning. Some of these goals may include wealth distribution during the individual's life. Potential beneficiaries may be a spouse, children, parents, and other dependents. The individual also may want to benefit one or more charitable organizations. The process of lifetime transfers differs from transfers after death, and this course explored both scenarios. As part of the coverage, the course looked into situations where the individual, or a family member/dependent, becomes incapacitated. These situations normally require special care as well as increased and long-term funding. Finally, the course covered several estate planning strategies, again, including those applicable to an individual's lifetime as well as following their death.

Estate Planning and Wealth Transfer

1. Collection

    1.1 Collect Quantitative Information

    1. Collect legal agreements and documents impacting estate planning strategies

1.2 Collect Qualitative Information

1. Identify the client’s estate planning objectives
2. Identify family dynamics and business relationships that could impact estate planning strategies
3. Assess the client’s attitudes and biases toward estate planning

2. Analysis

2.1 Assess the Client Situation

1. Project net worth at death
2. Analyze constraints to meeting the client’s estate planning objectives
3. Compare potential estate planning strategies

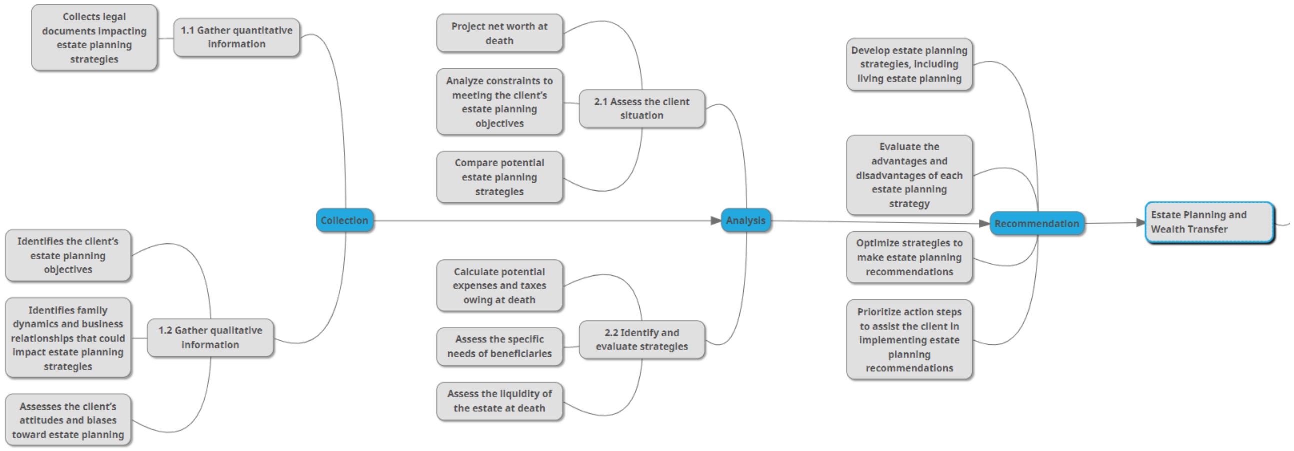
2.2 Identify and Evaluate Strategies

1. Calculate potential expenses and taxes owed at death
2. Assess the specific needs of beneficiaries
3. Assess the liquidity of the estate at death

3. Synthesis and Recommendation

1. Develop estate planning strategies, including living estate planning
2. Evaluate the advantages and disadvantages of each estate planning strategy
3. Optimize strategies to make estate planning recommendations
4. Prioritize action steps to assist the client in implementing estate planning recommendations

Estate Planning and Wealth Transfer



Chapter Review Answers

Chapter 1 Answers

1. What is an estate?
   An estate is all rights, titles and interests a person has in any property. It also includes all debts and liabilities. The person may be living or dead, and the term encompasses all owned property prior to death and distribution of that property.

2. What are three types of property and ownership arrangements?
   - Real: This is land and permanent (immovable) structures on it. This is sometimes called real estate and at other times referred to as immovable property. Although there are technical differences between the terms, we will refer to real estate or real property as the overall term.
   - Personal: Personal property may either be tangible or intangible. Tangible personal property refers to items, other than real property, that has a physical presence (i.e., can be touched) and has value. Intangible personal property is that which is other than real or tangible. This is property, such as securities, bank notes, and intellectual property (although this sometimes is considered as being in its own category), that has value as a result of legal, contractual rights. Securities sometimes also may be considered as having their own category.
   - Community: several states and a few territories (e.g., France, Brazil, U.S.) have a category of property ownership between spouses known as community property. Specific regulations differ, but generally, community property is all property acquired and held as part of the matrimonial estate. Within community property regimes, some property may be excluded or exempt.

3. What is an inheritance and what ownership rights does it involve?
   Inheritance is the receipt of property from an estate, often as a result of estate planning. It can include taking physical ownership of real and tangible property. It also may involve receiving legal and/or beneficial ownership of intangible property. This includes all rights, interests, and titles in the property. Legal ownership refers to the right to manage property, including the ability to transfer it from one person or entity to another. Beneficial (or equitable) ownership is the right to use and enjoy property. An individual may have one or both types of ownership, with heirs (i.e., those who inherit property as outright owners) having both.

4. How do present interest and future interest differ?
   - Present interest refers to beneficial ownership that allows a person to use the property immediately. In addition to situations where a person has outright (current) ownership, beneficiaries of a trust who receive current income from the trust (or can demand payments) are said to have a present interest in the trust assets.
   - Future interest is used when a person will have ownership but cannot use the property immediately. Beneficiaries in a will have a future interest in the property because they must wait until the testator dies before they inherit the property. Trust beneficiaries who receive trust assets after income from it terminates are said to have a future interest. A trust beneficiary who receives mandatory income payments

(or can demand those payments), as well as ultimately receiving the trust assets (i.e., corpus), has both a present and future interest.

5. What is common law and where is it applied?
   Common law, also known as English common law, is a legal system based on the common-law courts of England. The legal system found in most British Commonwealth (i.e., the Commonwealth) states (e.g., Australia, the Bahamas, Canada, Fiji, Malaysia, Malta, New Zealand, United Kingdom, and others) and the United States generally follow case law and precedent (with exceptions) going back to England over hundreds of years, and to some degree, based on laws dating from the Middle Ages.

6. What is civil law and where is it applied?
   Civil law dates back to Roman times and is embraced by many European and Scandinavian countries, especially France and Germany, as well as Brazil, Bulgaria, Chile and several Central and South American territories, Egypt, and others. While it's not important to know all about the two legal systems, you should recognize that territories in each system address estate planning in different ways. Civil law tends to be more prescriptive than common law. That is, it applies a greater amount of laws with specific steps and application. Common law, in general, allows a little more flexibility in interpretation and application of relevant regulations. Civil law tends to more specifically identify things such as who can inherit, laws of succession, compulsory/forced heirs, and the like.

7. What is probate and what property generally does or does not pass through it?
   Probate is the process of settling a decedent's estate. When an individual dies, the estate must go through the probate process, except for those assets that pass by law or will substitute/contract. Essentially, probate is a legal proceeding in which a decedent's will is reviewed by a court (e.g., probate court) that has legal authority over the settlement of the decedent's estate. The court determines the legality of the will and arranges for whomever and whatever may be necessary to carry out terms of the will. In cases where there is no will, or one does not apply (e.g., mandatory succession rules), the estate will be settled according to intestate succession rules. Generally, life insurance assets and other contracts that include a named beneficiary, pass outside the normal probate process. While the probate process is likely to incur expenses and will help identify taxable property, the probate estate is not identical to the taxable estate. Probate therefore refers to the settlement process rather than the determination of applicable taxes. Also note that not every territory requires a will to pass through a formal probate process

8. What is the purpose of a testamentary will and how may it be used?
   A will is a document (except in cases of a valid oral [noncupative] will) that specifies how the property owner wants his or her estate to be distributed at death. It can be used to identify someone to administer the estate (i.e., executor or personal representative) and identify a guardian/administrator for minor children. A will normally cannot be used to override applicable laws or will-substitute contracts. Not all territories recognize the following options, but a will may be legal/formal (i.e., written following applicable regulations, properly witnessed, notarized when required, and authorized or approved by an authorized individual or entity). Wills may, where allowed, be handwritten or oral. A territory may or may not honor either type of will. To be valid, a handwritten will must be complete, signed and include a creation date. Generally, a handwritten (holographic) will must be delivered to an authorized person, such as a notary or justice of the peace. Oral wills are seldom allowed and, when used, must be heard by witnesses (usually at least two).

9. When would a person use a living will or advance directive?
   A living will fits in the broader category of advance directives, which may include powers of attorney, health care proxies, health care directives, and advance health directives (and may go by other titles). Some territories give this type of document full legal status. In others, it is used more to provide guidance regarding the individual's desires but does not have actual legal status. Some territories do not recognize the validity of this type of document at all. The primary function of a living will (and alternatives) is to specify the course of treatment health care providers and caregivers should follow. It becomes especially useful in situations where the maker is incapacitated, and therefore unable to give personal guidance regarding what he or she wants to happen.

10. What are will substitutes and how do they impact potential probate estate property?
    Will substitutes are contracts that pass assets directly to a named beneficiary. Probably the most common and well-recognized such document is a life insurance contract. Most, if not all, territories consider life insurance contracts to be in a separate category. In many scenarios, proceeds from a life insurance policy are not considered part of the estate and pass outside probate and outside other succession laws directly to the named (also, nominated) beneficiary.

11. What is the simplest form of property ownership?
    The simplest form of property ownership is individual ownership. Full and complete ownership often is identified as fee simple property ownership (sometimes also known as a *freehold*). One individual and no one else is involved.

12. What are the types of joint property ownership?
    Joint ownership (also co-ownership, shared ownership or concurrent ownership) typically has two primary forms: joint tenancy and tenants in common. Neither form requires ownership to be between spouses. When spouses jointly own property they may do so using a form of joint tenancy with rights of survivorship known as tenants by the entirety. This arrangement is only available to spouses and like other forms of joint ownership that have rights of survivorship, cause the property to pass from the decedent to remaining owner automatically, without passing through probate. Another way of saying this is that each owner has an equal right to the entire property. Joint tenants own property equally, unless the owners hold the property as tenants in common. At the death of one owner, that owner's share of the property will pass to the other owner(s). Tenants in common may own property in unequal (proportionate) shares. Further, these owners may distribute their share of the property in any fashion they desire, without agreement by remaining owners. This arrangement does not come with rights of survivorship. As such, when one owner dies, his or her portion of the property passes to the decedent's estate and will be distributed according to the terms of the will. The remaining owners have no automatic right to the decedent's share of the property.
13. What is the primary identifying factor for community property?
    Community property is all property, unless otherwise declared as being separate, that is acquired after marriage. (including debts). This has implications for estate planning, and also while spouses are living.

14. What is the main characteristic of a forced heirship scheme?
    Property owners are not completely free to distribute estates as they wish. Why? There are rules against disinheriting certain kin—primarily the spouse, children, and grandchildren—and also potentially grandparents and other family members. The rules typically apply to the

estate as a whole, but it is possible that some assets may be excluded and distributed according to the desire of the decedent.

15. What makes a gift "complete"?
    Technically, a gift must be complete to qualify as a gift. Complete means the property owner has relinquished control over the property being transferred.

16. Would a donor who places an income-producing asset in a trust and directs income to be paid to another individual or entity be credited with making a completed gift?
    No. Even though the donor is providing for income to flow to the recipient, this is not a completed gift. The original owner has not relinquished control over the asset. He or she directed what was to happen to the income and reserved the right to retake the asset at some point in the future.

Chapter 2 Answers

1. What three questions can clients ask themselves to facilitate an end-of-life discussion?
    - What was the meaning of my life?
    - Did I make a difference in the world?
    - What is my legacy to the world?

2. What are some common estate planning objectives, especially for married couples?
    - Provide for loved ones. Financial security is one of the most important goals for most couples wanting to ensure that their loved ones are provided for when one of them dies or becomes incapacitated.
    - Minimize taxes. It may not be the primary goal, but it's certainly a common goal, so that more assets pass to heirs rather than the government if at all possible.
    - Protect assets passing to surviving spouses/heirs. Minimizing threats is mostly about keeping assets protected from creditors and any who would try to take over assets unscrupulously.
    - Make it simple and inexpensive. Make estate plans easy to follow for heirs (including the surviving spouse/partner) without undue costs, but not at the expense of accomplishing overall objectives.
    - Keep things private. Maintain privacy to the degree possible.
    - Have control over assets. Maintain control over assets to the maximum extent possible.
    - Plan for potential incapacity. Make arrangements to address myriad potential needs in the event one of the individuals becomes incapacitated in some way.
    - Manage assets. Put into place systems to assure positive financial management when one or both is no longer capable of managing family assets
    - .

3. What two questions can a financial planner ask to address potential concerns related to heirs who may not be in a position to take care of themselves?
    - Do any of the heirs/beneficiaries need protection, and if so, from whom?
        - This could be a situation where an elderly person is mentally incompetent, or nearly so; a minor who is likely to overspend inherited assets; creditors; even siblings and former spouses.
    - Who will act for the individual when he or she no longer is able to do so?

4. In addition to distributing assets to family members, what is a common desire and need for a

decedent to take care of family?
Many assets are illiquid, and the decedent want to provide adequate liquidity for the surviving spouse and children.

5. Why may forced heirship be a potential problem for surviving spouses?
In territories where children are prioritized over spouses, the surviving spouse may not have enough assets from the estate to keep taking care of the family and themselves. Recognizing potential difficulties, many territories' rules allow the surviving spouse to receive a larger portion of the estate. In turn, surviving spouses will be better able to support themselves along with the children.

6. What are three common needs parents may have for dependent children?
First, sufficient funds to provide for living expenses. Second, because minor children cannot (and usually will not be allowed to) manage money for themselves, a guardian or administrator to oversee the funds. Third, someone to care for and guide the children as they grow to majority and independence.

7. What action will most jurisdictions take to protect children's financial assets from their inheritance?
Most jurisdictions require a guardian or administrator to be appointed who can oversee funds for the benefit of the children. Usually, this is done under state supervision and requires regular reporting to the state or a designated agency.

8. What are six money myths children may believe that can harm them?
Money = happiness, money = love, money = power, money = freedom, money = self-worth, money = security.

9. One identified potential problem when HNWI's children inherit a large amount of property is called affluenza. What is affluenza and how can it be addressed?
Affluenza is a false sense of entitlement. To help overcome this, over the years, many HNW parents have attempted to instill core money values in their children. One such value is learning to give to others through charitable endeavors.

10. As a practical matter, what may parents do to help heirs handle their inheritance?
As a practical matter, parents also should consider establishing a trust, guardian, administrator, etc., to place some parameters around children's use of an inheritance—especially when they are first learning how to cope with the sudden money.

11. What are some of the top estate-related concerns of small business owners?
    - Continuing to develop and remain a profitable business
    - Management succession planning
    - Planning for later life
    - Engaging and developing the next generation
    - Ownership succession and developing responsible future owners
    - Identifying and maintaining family values
    - Extracting value from the business
    - Taxation

12. When developing a business succession plan, what points should be considered?
    - The successor; family member, business partner, other
    - Succession type; partial or full succession

- Timeframe
- Key personnel changes and skill retention strategies
- Restrictions
- Legal consideration; buy-sell agreement, reference to a will
- Risk management
- Communication strategy
- Financial considerations; retirement income, sale prices, tax implications

13. There are three consistent elements in most buy-sell agreements. What are they?
    - Who can buy the departing owner's share of the business
    - The circumstances that allow the share of the business to be sold, such as retirement, death, disability, or leaving the business
    - The price that will be paid for the share of the business

14. When the current environment is not especially conducive to selling the business, but that situation is anticipated to improve in the near future, what can surviving family members do to continue business operations for a period of time?
    One of the considerations may be to try selling the business prior to the owner's death. If the business cannot be sold, the family should have plans to close the business or perhaps hire someone (or a firm) to manage the business.

15. What are some common business objectives following the death of an owner?
    The first is to keep the business going. Depending on the business size, it's likely to have employees who would like to continue working. Also, the remaining owners almost certainly wish to continue earning an income from the business, as well as having the value of their ownership share increase. The family of the decedent also will have related concerns, chief of which is how they can recover the decedent's investment. Also, it's likely they were counting on an ongoing income stream from the business, and now they will be concerned that the income will cease. A well-constructed buy-sell agreement will address each of these concerns.
16. What is a common method to provide funding related to a buy-sell agreement?
    There are several ways to provide the funding, but one of the more common methods is through use of one or more life insurance policies. The business may own a policy on the owners, or each of the owners may own a policy on each of the other owners (e.g., entity or cross-purchase agreement, also known as a cross-option agreement). Regardless of the manner of life insurance policy ownership, the end result is the same: The money is made available for the remaining owners/corporation to purchase the decedent's business share from the surviving spouse/family. In doing so, each party's interests are supported. In lieu of life insurance, the business may establish a sinking fund to make the eventual purchase. Another alternative is to make installment payments from the business to the surviving spouse/family.

Chapter 3 Answers

1. What are common steps that should be part of most estate plans?
    - Create an inventory of what is owned and what is owed
    - Develop a contingency plan
    - Provide for children and dependents
    - Protect assets
    - Document wishes
    - Appoint fiduciaries/legal representatives

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2. When creating an inventory, in addition to identifying property, what types of things should the list include?
   An inventory should include things like account numbers, contact information, medical personnel, online login information (i.e., username, password and URL), as well as all physical property (real and personal) investment assets, and anything else of value. This list also should include current debts and related information (amounts owed, to whom, payments, etc.). It's a good idea to include contact information for financial and other advisors. The list, and supporting documents, should be kept in a secure location that can easily be accessed by surviving spouse, heirs, and legal representatives. The client should make a summary of the information and provide it to the people who should have the information.

3. What are four basic coverages of a will?
   - Specifying how the individual wants the estate to be distributed at death
   - Naming an executor (who will help administer the estate in accordance with the will)
   - Naming a guardian/administrator for young (minor) children
   - Revoking any previous versions of a will

4. In most territories, how may a will be used to disinherit a surviving spouse and/or children?
   Most territories will not allow this to happen and will override any will that attempts to do so.

5. What is a residuary clause, and why would one be included in a will?
   Having a residuary clause allows the individual to address any property that may have been forgotten, or arrives following death (e.g., an investment dividend, final payments from work, a car or other assets, etc.). The individual can insert a clause in the will stating that all that remains following payment of debts, etc., and specific amounts already identified in the will, should pass to a designated person or organization. It's a catch-all statement that keeps anything from falling into a place where the probate court will have to determine the distribution.

6. How likely is it for a will drafted in one territory to be completely valid in another territory (i.e., cross-border scenarios)?
   When working with cross-border and expatriate clients, if they have a will that was drafted in their home territory, it likely will not be completely valid in another territory. This often is the case, especially when succession laws (e.g., forced heirship) are not recognized in the home/other territory, but are a part of the current territory (and vice versa). As a result, one of the first steps when doing cross-border estate planning is for the client to have the will reviewed by a competent legal representative in the current territory. Commonly, at least some modifications will be required.

7. How does a trust divide property ownership?
   A trust will divide property into two categories: legal ownership and beneficial ownership. Legal ownership is vested in the trustee who is required to administer the trust assets (corpus), on behalf of the grantor, for the benefit of the beneficiary, who has beneficial ownership. As previously described, beneficiaries who must wait to receive the trust corpus are said to have a future interest, while those who can demand and receive current income are said to have a present interest.

8. What is a grantor trust and how does it compare to a non-grantor trust?
   A grantor trust is one in which the grantor (i.e., the individual creating and supplying trust assets) retains some degree of control over the trust. He or she may be a trustee and may also be the beneficiary. A non-grantor trust is one in which the trust creator gives up all right, title, and interest in the trust corpus. Therefore, assets are entirely owned by the trust. Grantor and non-grantor trusts normally will be treated differently for tax purposes, with non-grantor trust assets being taxed to the trust.

9. How may a trust be used to benefit a minor beneficiary or one who is unable to competently manage assets?
   A trust can designate a trustee who will oversee assets given to a minor child. It may also be useful when the child is not a minor, but incompetent to manage assets. A beneficiary who cannot manage assets may not be a child, but may be a parent, sibling or other, who may be elderly or simply unable to manage assets well. This is especially true with beneficiaries who may be physically (or mentally) disabled. Some territories allow for trusts to specifically benefit those who are disabled (e.g., special needs trust), and may provide tax or other incentives to make use of this tool.

10. What is a pourover will and how might it be used?
    When the grantor dies, it may be advantageous for him or her to insert a provision in the will that sends all assets (or at least those not otherwise distributed) into a trust. A will used for this purpose may be called a *pourover will*. Assets will “pour over” from the estate into the trust, and then be subject to terms of the trust.

11. Final expenses may be grouped into five broad categories. What are they?
    - Administrative
    - Death taxes
    - Debts and claims against the estate
    - Cash needs
    - Cash bequests

12. Why is cash (liquidity) needed by survivors?
    The expenses that the family will have to pay mount up quickly. Even though there has been a death, life must continue for survivors; all normal expenses continue, and end-of-life specific costs require money. It’s not uncommon, if death is preceded by a significant illness, for medical expenses to add up as well. Any of these in excess of state social security benefits or insurance must be paid. Additionally, settling the estate often requires payments of fees and taxes. Appraisals cost money, and appraisers don’t want to wait until the estate is settled to be compensated. The same is true with lawyers, accountants, and others involved in settling the estate.

13. How is the value of a gross estate determined?
    Expenses must be subtracted from the estate’s value. The gross estate is everything owned by the decedent. This can include all current assets, bank and investment accounts, at least some portion of jointly-held assets, amounts owed to the individual, but not yet paid, ongoing royalties, real estate rents, retirement accounts and similar continuing income streams, life insurance payable to the estate, and some policy situations where the decedent retained incidents of ownership (even when the proceeds go to a named beneficiary), revocable living trust assets, trust assets where the decedent was the beneficiary, real property, and business interests. Assets jointly owned with a spouse may be assessed at half the current market value. Other jointly held ownership arrangements will

be assessed based on the percentage contribution of each owner. So, if the decedent owned 60% of a property, that's the percentage of the value that will be included in his or her estate. If the decedent owned an asset and controlled it, the asset can be a part of the gross estate. To determine the value of a gross estate, add the value of all assets in which the decedent held incidents of ownership.

14. How does the probate estate differ from the gross estate?
    The gross estate is everything owned by the decedent. The probate estate includes only those assets that pass through probate. This means assets distributed according to a will or by the rules of intestacy. It does not include assets such as will substitutes, which can include life insurance to a named beneficiary, irrevocable trust assets, certain ownership titles, and other assets that pass according to law. The probate estate will often be smaller, sometimes quite a bit smaller, than the gross estate.

15. What is the taxable estate and how might it be settled?
    The taxable estate will vary based on includible assets, which varies by territory. Some assets may be assessed at higher rates than others—notably real estate. A territory may have tax rules that eliminate the value of some assets from taxation. Certain ownership provisions (e.g., how an asset is titled or owned) may reduce or eliminate potential taxes. Some assets are legislatively carved out of the taxable estate. Cross-border estates likely will experience taxation at different rates, perhaps on different assets. It's possible that a separate accounting will be required for each relevant territory. One of the questions that must be asked is who has jurisdiction. The answer will depend on the way taxes are assessed by applicable territories and the treaties in effect that reduce or eliminate double taxation. Often, an ongoing income stream is deemed the purview of the territory in which it is generated. This may result in taxation (income or estate) in that territory in addition to the country of last domicile. From the gross estate, subtract any amounts carved out by legislation (e.g., assets going directly to a spouse). Also, subtract debts and other expenses, which may include funeral expenses, excess medical bills, administrative expenses to settle the estate, outstanding mortgage and other debt amounts that must be settled. The value of an asset may require professional appraisal. Related expenses qualify as an administrative expense. The amount that remains is a net estate. Some territories exempt the value of certain assets, especially those going to a spouse or perhaps children, from taxation (or tax those assets at a different rate). After subtracting all expenses, nonincluded assets, and exemptions, what remains is the taxable estate. Remember, taxable amounts may vary in different territories as the estate is assessed; especially relevant in cross-border scenarios.

16. Must all debts be settled (fully paid) at the death?
    Settling debts and paying taxes are part of overall estate administration. One important factor to keep in mind is that not all debts must be settled at death. Sometimes, such as when a mortgage or other loan is jointly held, the remaining debtor can simply continue making payments, rather than pay off the entire loan immediately. Likewise, depending on rules within different territories, credit debts held solely by the decedent may not have to be repaid by survivors. They might decide to do so, but may not legally be required to settle all the decedent's debts. The personal representative or the courts should make this clear to surviving family. Some debt settlements may be negotiated by the surviving family to reduce overall amounts or extend repayment periods.

Chapter 4 Answers

1. What are two primary reasons for making an *inter vivos* gift/transfer?
   Lifetime, or *inter vivos*, transfers may have a primary purpose of removing assets from an estate. However, many times, an equally strong reason to make a gift is for the giver to be alive to see the recipient use the gift.

2. Who normally pays taxes related to giving or receiving a gift?
   Typically, the donor or gift-giver pays any taxes. However, sometimes the donee or recipient may have to pay any taxes due.

3. If an individual wants to reduce estate-related liabilities by giving an *inter vivos* gift, is there any possibility the gift may be recalled or brought back into the estate?
   Yes, many territories have a *lookback* period for when the gift giver dies within a certain period of years following the transfer. For example, the value of all gifts made within three years (or seven or other) of death may be recalled to be part of the estate valuation. Usually, a certain amount will be exempt from taxation regardless of the recipient. Likewise, gifts to a spouse or civil partner may well be exempt from taxes in full or part. Also, very small gifts often may be made with no tax implications.

4. What is a unified tax and how may it be applied?
   A number of territories have a unified gift and estate/inheritance tax. Where it exists, the tax applies to the value of the estate at death and to certain transfers or gifts made during the individual's lifetime. In a unified system, the value of lifetime gifts will be deducted from any estate tax exemption. As a result, it may be possible to give lifetime gifts with enough value that there is no estate tax exemption/exclusion left, and the entire taxable estate actually will be taxed.

5. What are some of the options a sole business-owner may use to transfer/distribute a business interest while he or she is living?
   A possible solution is for the owner to sell (e.g., as a going concern) or liquidate the business prior to death. This could be done as a transfer for value (e.g., purchase price = business's appraised fair market value), or, when appropriate, the owner might make a gift of the business. When making a gift, the most likely (but not the only possible) recipient will be a family member. Gifts to family will be subject to the territory's normal gifting rules, including potential taxation. If the owner *sells* the business to a family member at a discount, the difference between the discounted price and fair market value likely will be deemed a gift. The same probably will be true for any advantageous transfer methods used (e.g., discounted loan, favorable installment sale terms, etc.). One of the questions the owner and family member recipient must ask is whether the recipient is willing and capable of running the business. If not, an outright sale to a third party probably will be a better solution.

6. What are some available stock-based options for a sole proprietor who wants to gift a business to a family member?
   He or she may also want to shift the form of ownership to create different classes of ownership interest. This may mean (for example) reorganizing as a closely held corporation that can issue stock. Doing this will allow the owner to gradually transfer ownership, while maintaining a degree of control during the transfer period. One possible arrangement would be to create two classes of stock: common and preferred. Common stock has voting rights and could remain with the current owner. Preferred stock normally has no voting rights and could be gifted to the family member. Alternatively, the family member could be given a non-

majority share of common stock, and the current owner could keep preferred stock as a way to guarantee ongoing income. (Holders of preferred stock must be paid all dividends/income due them prior to the corporation paying any dividends to other shareholders.) This would begin the transfer process, reduce financial exposure to the owner's estate, and allow continued control of the business by the current owner.

7. What is a personal representative (PR) and what are some of his or her primary functions?
   Whether or not a decedent has left a valid will, the estate settlement process will require a personal representative (PR—also known as an executor/executrix or administrator). A well-constructed will should name the PR, who the court can approve, but when the individual died intestate, the court will appoint a PR or administrator. Whoever is chosen as PR will be given legal authorization to represent and act on behalf of the estate. One of the first duties of the PR is to determine (and seek out) the decedent's assets. This means the PR may need to contact banks and financial institutions and notify them of the person's death. He or she will also provide authorization to become the legal point of contact moving forward. During this part of the process, the PR will need to collect any money held in accounts solely titled in the decedent's name. The PR will also want to ensure the decedent's real and personal property are protected as much as possible against the possibility of theft or vandalism. The PR will collect amounts that may be due the decedent. This can include rents, royalties, debt repayments, and the like. He or she also will need to contact sources that provide ongoing income streams and inform them of the death, along with any change in payment information. The PR will need to ensure that required debt and other payments owed by the decedent get paid as agreed. He or she will need to notify creditors with all relevant information, including instructions for filing a claim against the estate. The PR also will have to ensure assets are distributed according to a valid will or applicable statutes.

8. Probate can be a positive process used to effectively administer a decedent's estate. However, it also can have some negatives associated with it. What are some of the negative aspects of probate?
   First, probate can be expensive. All the court costs, legal fees, assessors, accountants, the personal representative, and related fees can cost quite a lot of money. These expenses are paid prior to distribution of assets and may result in a smaller estate to be distributed. As a result, most people want to keep the probate process and its expenses to a minimum. Also, probate takes time; the process of determining asset values, applicable heirs, etc., can be time-consuming. The resulting delay in distribution can become frustrating for heirs. Probate records generally are considered public information. This means interested parties can access much of the information and make it public

9. What options may HNWI and heirs use to protect their privacy as part of estate distribution?
   Heirs of HNWI make more lucrative targets than those with fewer financial assets. To protect against this, HNWI may find it reasonable to have assets flow into a trust and name a reliable, often professional, trustee. Additionally, they may use foreign (e.g., offshore) corporations to hold assets, or perhaps make use of domestic corporate (or other) entities that provide a degree of security and privacy. One of the reasons this can work is that the heirs don't actually own the assets—the corporation (or other entity) does. Proper documentation ensures the heirs access to the assets, and they will be protected from predatory individuals in the process.

10. What categories of family members may be considered mandatory heirs in a forced heirship

scheme?
Children of the decedent normally will be considered to be primary heirs. The surviving spouse also often is included. Mandatory heirs may extend beyond immediate family members to include parents, grandparents, siblings, cousins, and other related persons. Many times there is an order to how inheritance is distributed. The first, and largest share often going to the first-born (often male), then to the next in line, and so on. It's entirely possible that, under such a plan, those in a lower category may receive no inheritance, as the assets already will have been fully distributed.

11. Three main options exist that may circumvent forced heirship distribution schemes. What are they?
    The first is through making lifetime (*inter vivos*) transfers. Lifetime transfers work because any assets that are gifted (following proper procedures) no longer are part of the estate, therefore, at death, it's not possible for them to be included in a forced heirship scheme. A second option is to create a trust (*waqf* in Islam). Remembering that not all territories recognize trusts, it may be possible in some territories to circumvent forced heirship rules by using a trust. The trust can nominate beneficiaries who, as legal owners, will receive trust assets, bypassing forced heirship distribution. Some territories, however, specifically deny the right of a trust to bypass the heirship rules. A third possibility is to establish a foreign company to own property. Property transferred to a foreign company (e.g., offshore) is likely not to be impacted by a territory's forced heirship rules.

12. What is usufruct and how may it apply to estate planning?
    Usufruct technically refers to the ability of a person to use the property of another person, without changing the character of the property. It may be applied to use of land, buildings, and/or movable objects. In some circumstances, it can even extend to using money and other assets that may be totally consumed by the user (i.e., usufructuary). Usufruct is not specifically limited to surviving spouses, but it certainly can be applied. Usufruct can allow a surviving spouse to live in the family home, use community property assets, and the like. The right normally terminates at the earlier of remarriage or death. As such, usufruct is not necessarily as beneficial as outright inheritance and ownership, but it does provide a degree of security to the surviving spouse.

Chapter 5 Answers

1. What is incapacity and how may it impact an individual?
   When an individual suffers from an incapacity, he or she has a disability—physical or mental—that impedes the ability to think and act as desired. Incapacity also can make a person legally ineligible to handle their own affairs. This most often is caused by experiencing a lack of mental fitness. The person is unable to process information appropriately or understand the consequences of their actions. When a person is judged to be incompetent and has not made prior arrangements, a guardian or administrator often is chosen as a helper, and this arrangement may not be wholly satisfactory to the individual. As is true of dying intestate, the state will make decisions on behalf of the individual and do so by following predetermined guidelines. This may result in loss of personal freedom, and having a caregiver put in charge who is unknown by the individual or the family. Sometimes, in the legal realm, the incapacitated person no longer has the right to represent themselves. This, as is easily understood, is extremely disruptive to the individual, as well as for close family members.

2. What are core elements of a medical workup for mild cognitive impairment (MCI)?
    - Thorough medical history
    - Assessment of independent function and daily activities
    - Input from a family member or trusted friend
    - Assessment of mental status
    - In-office neurological examination
    - Evaluation of mood (especially to detect depression)
    - Laboratory tests (perhaps including brain imaging)

3. What are some key symptoms of MCI?
    - Forgetting things more often
    - Forgetting important events such as appointments or social engagements
    - Losing a train of thought or conversation thread
    - Feeling overwhelmed by decision-making, planning steps to accomplish a task or interpreting instructions
    - Having trouble finding the way around familiar environments
    - Becoming more impulsive or showing increasingly poor judgment
    - Family and friends notice these changes

4. As a financial planner, what can you do if you recognize that a client is experiencing MCI?
   When working with a client, you may notice some signs of MCI. If you do, you can suggest to the individual, and perhaps a trusted family member or other individual, that an evaluation, including some or all of the above, might be beneficial. When a client experiences mild or full-scale dementia, it will change your relationship with them—both legally and professionally. If you do not identify suspected incapacity to appropriate individuals (e.g., family, supervisors, related professionals), you may become legally liable for your actions. This is especially true if you are deemed to have taken advantage of the diminished mental capacity of the individual. Further, as a trusted advisor, you may be able to alert the client and/or family to a condition that has the potential to become critically disruptive.

5. What are the stages through which cognitive impairment can pass?
    - No impairment
    - Questionable impairment
    - Mild impairment
    - Moderate impairment
    - Severe impairment

6. What are some of the advance directives (legal documents) that can be used to prepare for the possibility of incapacity?
    - Durable or enduring power of attorney (POA)
    - Health care proxy
    - Health care/medical POA
    - Springing POA
    - Living will
    - Revocable living trust

7. Why is a regular POA not a good choice when a person becomes incapacitated?
   A normal power of attorney (POA) ceases to function when the principal becomes incapacitated. This defeats the purpose of having one in the event of incapacity. A better choice is a durable power or springing power.

Chapter 6 Answers

1. What are six estate planning concerns a financial planner should be ready to address?
    - Lack of liquidity
        - Need to have sufficient cash to meet settlement costs, taxes, and other final expenses
    - Improper disposition of assets
        - Preventing assets from going to wrong people, at the wrong time, or in the wrong manner
    - Inadequate income or capital
        - Need to provide for ongoing retirement expenses, special needs (see below), the client’s disability or incapacity, family living expenses after the individual’s death
    - Asset values destabilized and not maximized
        - Desire to keep business valuations as high as possible and assets distributed in ways that do not unnecessarily reduce their value
    - Excessive taxes and transfer/distribution costs
        - Keep final expenses and taxes to a minimum
    - Special needs
        - Provide ongoing care for a spouse who is not financially capable, children or parents who are not able to care for themselves (e.g., mental or physical disability), support for exceptionally gifted children

2. What impact can grief have on a surviving spouse’s ability to think and make decisions?
   A surviving spouse will enter a period of grieving. The exact parameters of grief and coping methods are completely personal and individual. That said, most people share some degree of similar experiences during this period. Grief—especially when it is extreme, as can be the case when a spouse dies—has an impact on how the surviving spouse thinks and feels. Mental clarity often is diminished for a time, and it can become difficult even to get through each day. The surviving spouse may experience many emotions that swirl around and can resurface multiple times.

3. What duties or responsibilities may a surviving spouse have as part of estate settlement?
   Financially, planning can include life insurance policy documentation, including beneficiary arrangements, insurer contact information, policy numbers, and the like (to file claims and possibly to cancel policies). The surviving spouse will need to know which other insurance policies should be continued and paid, and which should be terminated. The same is true with credit accounts, such as personal loans, mortgages, credit card accounts, car loans, etc. The spouse will need to know about all investment and banking accounts, and how to access them, remembering that territorial succession rules and legal beneficiary arrangements may impact the ability to have access to these accounts. This also will be true with ongoing retirement benefits and any other social security benefits. Some bills will have to be paid immediately, and this information should readily be available to the surviving spouse. The surviving spouse will have to obtain documentation that the decedent has died. This may be needed to present to any number of institutions, so multiple copies of such certificates of death probably will be necessary. Requirements in this area vary by territory and by institution. In some cases, papers must be in legal form and signed by appropriate authorities. It may be necessary for the surviving spouse to retitle the family house and perhaps a continuing mortgage in his or her name. The same may be true for other assets, such as a car, land, and financial accounts. Having a trusted lawyer and financial advisor on board will be helpful in this process.

4. What are some decisions that should not be made immediately following death of a spouse?
   There are a few things that should *not* be done immediately following the death of a spouse. These things include selling the house or other property, and giving away cash or other assets (even to children). The surviving spouse should be careful not to make any major financial, legal, or lifestyle change for a period of time (e.g., at least six months to one year); not succumbing to pressure tactics by anyone who wants to attach available assets. Sometimes this can be done by an otherwise trusted individual, so extra care may be needed (another good reason to have a strong support network, including legal and financial advisors).
5. What is the biggest potential difficulty an unmarried domestic partner may face when their partner dies and what can be done to address these concerns?
   An unmarried domestic partner may not have the same rights or support network as a surviving spouse. In general, an unmarried partner will require at least as much, if not more, specific estate planning clarity and documentation as does a surviving spouse. The decedent's instructions in a will must specify the partner (when desired). The same is true for beneficiary arrangements on life insurance policies, continuing retirement income plans, and similar. Not all territories acknowledge or accept the legality of unmarried partnership arrangements. As a result, some spousal-type planning will not work in these territories. For example, it's entirely possible that, even though a decedent's will identifies the partner as a legal beneficiary, territorial succession rules may invalidate that designation. Sometimes this can be overcome by other contractual arrangements (e.g., life insurance beneficiary nomination). Where territorial laws allow all or some portion of a decedent's estate to pass to a surviving spouse tax-free, a surviving partner is unlikely to receive the same benefit. As in other ways, adequate life insurance with appropriate beneficiary designations can be helpful to provide the funding necessary to pay taxes and other expenses.

6. What is a situation in which ex-spouses may need to work together to do estate planning?
   One situation is the desire, need, or requirement to provide for children from the former marriage. These children may or may not be included in any forced heirship regimes. If they are not, they may be in danger of being disinherited. Most times, this is not the desire of the ex-spouses, nor is it in the children's best interest. Appropriate documentation in an applicable will is an important place to begin. Both spouses should include the children, often by name, in their respective wills. Care will be needed to provide for other children, including those from any current marriage. Where possible, the parents may wish to structure a trust to provide for the children. This is another scenario where proper beneficiary designations, including naming an administrator/guardian for the children, may solve many problems. Legal determinations from divorce proceedings may require a specific irrevocable beneficiary designation or similar for the benefit of the children. This will have to be included in estate planning considerations. Depending on the relationship between the ex-spouses, multiple meetings, perhaps both separately and together, may be required to make the necessary arrangements.

7. What must be done for a gift to be considered a true gift?
   To be a true gift, the donor has to relinquish control of the asset. He or she sometimes may retain an interest in the asset (e.g., income for a period of time), but overall, when a person gives away an asset, he or she gives away all rights associated with the asset.

8. What is the function of a special needs trust and, where allowed, how may it be used?
   A special needs trust, as the name implies, is a vehicle to hold cash or other assets that will be used to pay for necessary care, housing and other expenses, and provide spending

money for the beneficiary. It’s possible, by placing assets in the trust, the beneficiary will retain the ability to receive additional government-provided aid that might not be available if the funds were given directly to the individual. Typically, a trustee will oversee how trust assets are distributed, including paying for caregivers, medical needs, housing, education, and other expenses. Government funds also may be available to provide a portion of the necessary financial support. The financial planner and family should use care in establishing the trust (or other) vehicle to ensure it is done in such a way as to receive all potential tax and other benefits and contains no provisions that may stand in the way of accomplishing its purpose.

9. What must be true for an intrafamily loan to be considered a legitimate loan?
   To be a loan, a financial transfer must have a legally recognized agreement, a stated rate of interest (which, in some cases in certain territories, may be 0%), and a repayment period with minimum required payment amounts. In other words, the requirements for an intrafamily loan basically are the same as for a non-intra-family loan.

10. What are some of the differences between an intrafamily loan and a commercial loan, and how may this benefit a family?
    An intrafamily loan can be a little different from a nonfamily/commercial loan. For one, the interest rate charged can be quite a bit lower. The government may have regulations regarding how low the rate can be, but it’s almost always lower than typically available on the open market. The repayment period also can be extended beyond what normally would be the case, and minimum required payments may be lower, too. Additionally, it should be noted that repayment amounts stay in the family (e.g., from the child to the parent), and can be used to increase cash flow or for whatever purpose the parent wants to make of it. When an intrafamily loan is used to transfer a family business, house, farm, or other real property from parent to child, it has the additional benefit of keeping the asset in the family. Also, an intrafamily transfer/loan effectively freezes the asset’s value as of the execution of the transfer.

11. What are two reasons an heir might want to disclaim an inheritance?
    There may be many reasons, two of which are associated debt and extreme inconvenience. When a person inherits an asset, often they also inherit any debt associated with that asset. Sometimes the debt can be quite large; large enough that the positive value of the asset is overshadowed by the debt. As a result, the beneficiary may decide not to accept the asset and thereby avoid inheriting the debt. A second reason used to disclaim an inheritance is inconvenience. This is most likely to occur in cross-border situations, but also may be relevant within a territory. A potential heir may live on one side of the territory, and the business he or she has inherited is on the other side. Perhaps the real property (e.g., house, farm, etc.) is so far from the heir that he or she cannot manage it. Perhaps the heir has a life and job in a city that will not allow them to easily interact with the inherited property.

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