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Advanced Estate Planning Concepts for Women

As you plan your estate, it is important to consider the tax implications. This can range from planning for the income tax basis of your property, to the gift tax, estate tax, and generation-skipping transfer tax potentially applicable to transfers of your property.

Statistically speaking, women live longer than men; if you're married, that means that the odds are that you're going to outlive your husband. That's significant for a couple of reasons. First, it means that if your husband dies before you, you'll likely inherit his estate. More importantly, though, it means that to a large extent, you'll probably have the last word about the final disposition of all of the assets you've accumulated during your marriage. But advanced estate planning isn't just for women who are or were married. You'll want to consider whether these concepts and strategies apply to your specific circumstances.

Transfer taxes

When you transfer your property during your lifetime or at your death, your transfers may be subject to federal gift tax, federal estate tax, and federal generation-skipping transfer (GST) tax. (The top estate and gift tax rate is 40%, and the GST tax rate is 40%.) Your transfers may also be subject to state taxes.

Federal gift tax

Gifts you make during your lifetime may be subject to federal gift tax. Not all gifts are subject to the tax, however. You can make annual tax-free gifts of up to $14,000 per recipient. Married couples can effectively make annual tax-free gifts of up to $28,000 per recipient. You can also make tax-free gifts for qualifying expenses paid directly to educational or medical services providers. And you can also make deductible transfers to your spouse and to charity. There is a basic exclusion amount that protects a total of up to $5,340,000 (in 2014, $5,250,000 in 2013) from gift tax and estate tax.

Federal estate tax

Property you own at death is subject to federal estate tax. As with the gift tax, you can make deductible transfers to your spouse and to charity, and there is a basic exclusion amount that protects up to $5,340,000 (in 2014, $5,250,000 in 2013) from tax.

Portability

The estate of someone who dies in 2011 or later can elect to transfer any unused applicable exclusion amount to his or her surviving spouse (a concept referred to as portability). The surviving spouse can use this deceased spousal unused exclusion amount (DSUEA), along with the surviving spouse's own basic exclusion amount, for federal gift and estate tax purposes. For example, if someone dies in 2011 and the estate elects to transfer $5,000,000 of the unused exclusion to the surviving spouse, the surviving spouse effectively has an applicable exclusion amount of $10,340,000 to shelter transfers from federal gift or estate tax in 2014.

Federal generation-skipping transfer (GST) tax

The federal GST tax generally applies if you transfer property to a person two or more generations younger than you (for example, a grandchild). The GST tax may apply in addition to any gift or estate tax. Similar to the gift tax provisions above, annual exclusions and exclusions for qualifying educational and medical expenses are available for GST tax. You can protect up to $5,340,000 (in 2014, $5,250,000 in 2013) with the GST tax exemption.

Indexing for inflation

The annual gift tax exclusion, the gift tax and estate tax basic exclusion amount, and the GST tax exemption are all indexed for inflation and may increase in future years.

Income tax basis

Generally, if you give property during your life, your basis (generally, what you paid for the property, with certain up or down adjustments) in the property for federal income tax purposes is carried over to the person who receives the gift. So, if you give your $1 million home that you purchased for $50,000 to your brother, your $50,000 basis carries over to your brother--if he sells the house immediately, income tax will be due on the resulting gain.

Women live an average of 4.8 years longer than men.* That's important because it means that there's a greater chance that you'll need your assets to last for a longer period of time. Keep this in mind when you consider making lifetime gifts. Property you give away is no longer available to you.

****National Vital Statistics Report, Volume 61, Number 4, May 2013.***

In contrast, if you leave property to your heirs at death, they get a "stepped-up" (or "stepped-down") basis in the property equal to the property's fair market value at the time of your death. So, if the home that you purchased for $50,000 is worth $1 million when you die, your heirs get the property with a basis of $1 million. If they then sell the home for $1 million, they pay no federal income tax.

Lifetime giving

Making gifts during one's life is a common estate planning strategy that can also serve to minimize transfer taxes. One way to do this is to take advantage of the annual gift tax exclusion, which lets you give up to $14,000 to as many individuals as you want gift tax free in 2013 and 2014. As noted above, there are several other gift tax exclusions and deductions that you can take advantage of. In addition, when you gift property that is expected to appreciate in value, you remove the future appreciation from your taxable estate. In some cases, it may even make sense to make taxable gifts to remove the gift tax from your taxable estate as well.

Trusts

There are a number of trusts that are often used in estate planning. Here is a quick look at a few of them.

- **Revocable trust.** You retain the right to change or revoke a revocable trust. A revocable trust can allow you to try out a trust, provide for management of your property in case of your incapacity, and avoid probate at your death.
- **Marital trusts.** A marital trust is designed to qualify for the marital deduction. Typically, one spouse gives the other spouse an income interest for life, the right to access principal in certain circumstances, and the right to designate who receives the trust property at his or her death. In a QTIP variation, the spouse who created the trust can retain the right to control who ultimately receives the trust property when the other spouse dies. A marital trust is included in the gross estate of the spouse with the income interest for life.
- **Credit shelter bypass trust.** The first spouse to die creates a trust that is sheltered by his or her applicable exclusion amount. The surviving spouse may be given interests in the trust, but the interests are limited enough that the trust is not included in his or her gross estate.
- **Grantor retained annuity trust (GRAT).** You retain a right to a fixed stream of annuity payments for a number of years, after which the remainder passes to your beneficiaries, such as your children. Your gift of a remainder interest is discounted for gift tax purposes.
- **Charitable remainder unitrust (CRUT).** You retain a stream of payments for a number of years (or for life), after which the remainder passes to charity. You receive a current charitable deduction for the gift of the remainder interest.
- **Charitable lead annuity trust (CLAT).** A fixed stream of annuity payments benefits a charity for a number of years, after which the remainder passes to your noncharitable beneficiaries, such as your children. Your gift of a remainder interest is discounted for gift tax purposes.

Life insurance

Life insurance plays a part in many estate plans. In a small estate, life insurance may actually create the estate and be the primary financial resource for your surviving family members. Life insurance can also be used to provide liquidity for your estate, for example, by providing the cash to pay final expenses, outstanding debts, and taxes, so that other assets don't have to be liquidated to pay these expenses. Life insurance proceeds can generally be received income tax free.

Life insurance that you own on your own life will generally be included in your gross estate for federal estate tax purposes. However, it is possible to use an **irrevocable life insurance trust (ILIT)** to keep the life insurance proceeds out of your gross estate.

With an ILIT, you create an irrevocable trust that buys and owns the life insurance policy. You make cash gifts to the trust, which the trust uses to pay the policy premiums. (The trust beneficiaries are offered a limited period of time to withdraw the cash gifts.) If structured properly, the trust receives the life insurance proceeds when you die, tax free, and distributes the funds according to the terms of the trust.

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