PUBLICATION

Estate Planning: More Important Than Ever

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As we approach the holiday season, our focus naturally turns to loved ones. This special time of the year traditionally presents an ideal occasion for you to express that love by updating your estate plan.

This year, however, the holiday season is inextricably mixed with devastating economic circumstances, as well as with uncertainties that necessarily will follow the November 4 elections regardless of one's political persuasions. One such uncertainty following the elections is the possible introduction of comprehensive tax legislation which, if passed, could compromise or eliminate currently available planning opportunities.

These present circumstances are a sharp reminder that a well-planned estate is more important than ever in the event of your death or incapacity. Your planning this year will be especially appreciated as a most heartfelt and invaluable gift which is designed to save time, money, taxes and trouble for your loved ones.

I. Important Non-Tax Reasons for Updating Your Estate Plan:

Many clients believe that estate planning is only relevant to help them avoid estate and inheritance taxes; however, there are a myriad of other reasons for estate planning. If any of the following have occurred since your last estate planning update, you should consider modifications to your plan:

- Material changes in your financial condition.
- You have married, with or without a prenuptial agreement. This may require the inclusion of particular testamentary provisions for a new spouse. In some states, marriage invalidates a former will.
- Marriage, divorce, or death of a child (or the former spouse of a child), particularly where such a person is named as an executor, personal representative, trustee, guardian, conservator, attorney-in-fact, health care proxy, or other type of fiduciary.
- Birth of a child or a grandchild. Consider specific bequests, § 529 college savings plans or establishing a trust.
- Divorce. Be certain beneficiary designations are modified so that assets do not pass to an unintended beneficiary, such as an ex-spouse.
- Relocation or other change of circumstances of persons named as guardians for minors or as executors or trustees. Some states require that an executor be a resident of the state where probate will take place.
- Change in family circumstances. Certain events may warrant changing testamentary provisions from outright disposition to disposition in trust. Factors indicating the need for a trust may include a lack of maturity or financial management skills, marital instability, concerns due to aging and potential senility, alcohol or substance abuse, and the preservation of government benefits or creditor concerns for beneficiaries who have special health needs. These same considerations might call into question the appointment of an executor, trustee, guardian or other fiduciary.
- Retirement or change in job that causes a change in employment benefits.
- Acquisition of new insurance. Assure the ownership and beneficiary designations coordinate to make an effective estate plan (i.e., consider whether the insurance should be acquired by or transferred to a trust).

- Receipt or expected receipt of an inheritance. Consider the possibility of using disclaimers in order to minimize the impact of inheritance on your own estate.
- Acquisitions of a major asset such as a new home (i.e., consider how title should be held).
- Acquisition of a business interest and the implementation of buy-sell agreements.
- Sale or disposition of an asset that was specifically bequeathed in your Will. This may skew the apportionment among beneficiaries with unintended consequences.
- Creditor issues that may impact planning.
- Forced heirship rules.

Please remember that proper estate planning should also include efforts to avoid conservatorship or interdiction and related problems in the event of incapacity…not just planning for what happens at death. The public drama surrounding end-of-life decisions in the Terri Schiavo case in 2005 should be a constant reminder of the importance of executing durable powers of attorney, powers of attorney for health care, living wills and advance care directives. It is important that our loved ones know our wishes in the event of our incapacity.

II. Federal and Estate Gift Tax Issues

Possible Federal Estate Tax Repeal

You probably have heard of proposals to eliminate the federal estate tax, or raise the federal estate tax exemption so that fewer clients would need to be concerned with the 45% estate tax now imposed on estates over the current exemption amount. As you know, the efforts over the past several years for a permanent repeal of the estate tax stalled in Congress. Certainly, the future of the federal estate tax will be largely impacted by the November 4 elections.

The federal estate tax exemption is at $2 million for the remainder of 2008, and will increase to $3.5 million in 2009. The federal estate tax is scheduled for repeal in 2010, and then re-imposed in 2011 with an exemption of $1 million, adjusted for inflation. Both presidential candidates favor retaining the estate tax with particular modifications. Complete permanent repeal of the tax during the next several years seems extremely unlikely. In light of this political uncertainty and Congress' inability so far to produce legislation, we do not advise that clients put off estate planning in order to "see what happens."

Gifts to Individuals and Charities

- Currently, annual exclusion gifts that are exempt from federal gift tax total $12,000 per donee annually. However, payments made directly to an educational institution (this does not include 529 education accounts or Coverdell Education Savings Accounts), as well as payments made directly to a health care provider for the benefit of a child, grandchild or other person (including non-family members), do not count against the $12,000 per donee exempt amount and are unlimited in amount. Such payments for educational and health care purposes can be powerful tools for reducing the size of your estate without using any of your lifetime federal gift tax exemption (currently such exemption is set at $1 million and is not scheduled to increase).
- The $12,000 per donee annual exclusion for gifts is scheduled to increase to $13,000 beginning in 2009 due to inflation adjustments.
- The Emergency Economic Stabilization Act of 2008, signed by the President on October 3, extends for 2008 and 2009 a provision that allows tax-free treatment of distributions from traditional or Roth IRAs if the taxpayer donates the distribution to charity. A taxpayer may exclude up to $100,000 of qualified charitable distributions from gross income in a tax year. Such a distribution will count toward the IRA owner's minimum required distribution for the year of the distribution. To qualify, the charitable distribution must meet the following criteria:

- The distribution is made on or after the date on which the IRA owner has reached age 70 ½; and
- The IRA trustee makes the distribution directly to a charitable organization. For this purpose, charitable organization does not include a private foundation under Code Section 509(a)(3) or a donor advised fund under Code Section 4966(d)(2).

III. Some State-Specific Issues

Tennessee

Gap Problem. Another reason for you to presently focus on estate planning is the so-called "gap" problem that exists in Tennessee and some other states. This gap problem does not apply to residents of Alabama, Georgia, Louisiana and Mississippi, but could apply to any other state that has a separate inheritance or estate tax. The current federal estate tax exemption is $2 million. There is currently a gap between the federal estate tax exemption and the state exemption level available in gap states such as Tennessee. Formulas in estate planning instruments often need to be modified to avoid paying a state inheritance tax on this gap amount and/or avoid wasting the amount of the federal exemption over the state exemption. If your estate planning documents have not been reviewed in light of this potential "gap" trap, we suggest that you have your lawyer review your documents for this particular problem.

Tennessee Investment Services Act of 2007. An interesting new estate planning tool was created by virtue of the Tennessee Investment Services Act of 2007 (the TIS Act), which became effective July 1, 2007. The TIS Act attempts to provide protection from creditors by allowing the creation of self-settled, asset protection trusts referred to as "Investment Services Trusts" (IST). The IST must meet certain statutory requirements. In most instances, transfers to the IST cannot be attached by creditors unless the creditor makes a claim under the Uniform Fraudulent Transfer Act. Creditors also cannot make claims against a trustee or any person involved in the counseling, drafting, preparation, execution, and funding of the IST. We strongly caution you to consult with estate planning counsel so that you can more fully understand what these trusts are, the protection that they provide, and any potential downside to the creation of such a trust.

Alabama

Uniform Estate Tax Apportionment Act. The Alabama Uniform Estate Tax Apportionment Act (ETAA) became effective on October 1, 2007 and applies generally to persons dying after December 31, 2007. The issue of estate tax apportionment concerns the source of payment of estate taxes and, thus, the beneficiaries who will bear the burden of the tax. Prior to the ETAA, Alabama law provided that estate tax was to be paid from the residue (i.e., the estate assets remaining after any specific bequests of cash, personal property, real estate, etc.) of an estate. While there are federal exceptions to this general rule (i.e., right of recovery for estate taxes attributable to certain marital trusts and trusts in which the grantor retains certain powers or interests), the prior law sometimes caused inequitable or unintended results. For example, if a person received property by beneficiary designation, specific bequest or right of survivorship, he or she would not have to pay estate taxes on the property. Rather, the beneficiaries of the residuary estate had to pay the estate tax attributable to such property. Under the ETAA, the apportionment rules apply only if a testator does not make a provision in the Will regarding how estate taxes are to be apportioned. The ETAA rules will apportion the estate tax among the beneficiaries of the estate, essentially on the basis of their shares in the net taxable estate, which will include specific bequests, joint tenancy assets, retirement accounts, and life insurance. This significant law may have substantial impact upon some clients' estate plans.

Louisiana

Succession Opening Requirements. Years ago, the Louisiana legislature repealed the Louisiana inheritance tax for deaths occurring after June 30, 2004, as long as the succession was judicially opened within nine

months of death. In 2007, Louisiana removed the requirement that the succession be judicially opened within nine months of death, effective January 1, 2008. If Louisiana inheritance tax was paid by the estate of an individual dying after June 30, 2004 because the succession was not judicially opened within the nine-month period, a claim for refund may be filed between August 1, 2008 and December 31, 2009.

Recently, the Louisiana legislature took another step toward full repeal by repealing the Louisiana inheritance tax provisions in their entirety, effective January 1, 2010. By doing so, the legislature intended to repeal the Louisiana inheritance tax for deaths occurring prior to July 1, 2004. Prior to this repeal, the Louisiana inheritance tax still applied to deaths occurring prior to July 1, 2004. Despite the legislature's intent, a technical application of the repeal does not result in full repeal of Louisiana's inheritance taxes on pre-July 1, 2004 deaths until December 31, 2011, not January 1, 2010, as intended. It is anticipated that the Louisiana Department of Revenue will soon issue guidance to clarify this gap left by the Louisiana legislature's imprecise drafting.

Gift Tax Repeal. The Louisiana legislature also repealed the Louisiana gift tax for gifts made on or after July 1, 2008.

Georgia

Georgia Revised Uniform Anatomical Gift Act. Effective July 1, 2008, this statute, replacing the prior one, is intended to respond to the need for increased organ donation. The act expands the class of persons authorized to consent to a gift after death when a donor has not made a written declaration. The new statute presumes that an agent under an Advance Directive for Health Care or durable power of attorney has the power to make a gift unless prohibited by the instrument from doing so.

Uniform Prudent Management of Institutional Funds Act (UPMIFA). Effective July 1, 2008, this statute modernizes the rules governing the management and investment of funds held by nonprofit institutions. It incorporates the more easily understood "prudent investor" standard and requires a charitable entity to follow the intent of the donor, whether expressed in the gift instrument or a separate written agreement. The previous statute prohibited institutional investors from spending the principal of an endowed fund if its value fell below the value of the property when originally given to the institution (the "historic dollar value"). Now the institution is given a more flexible standard, and directed to focus on donor intent and what is prudent for the purposes and duration of the fund.

Mississippi

Estate Tax Reminder. There are no Mississippi state estate taxes for decedents dying on or after January 1, 2005. The Mississippi state estate tax was tied to the federal state death tax credit which was repealed in 2005. If you have not already updated your estate planning documents to reflect this change in the law, please contact your estate planning professional.