
VIRGINIA ESTATE
& TRUST LAW

Estate Planning and Estate Administration Case Studies: Best Practices to Avoid Unanticipated Outcomes

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Agenda

Case Studies

- #1: Failing to Coordinate Asset Titling, Beneficiary Designations, TODs
- #2: Failing to Obtain Holistic Advice
- #3: No Estate Plan & Challenging Assets
- #4: Confusing "Fair" with Equal
- #5: Declining Mental Capacity
- #6: Lost Will
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- #8: Assuming the Conclusion
- #9: Missed Planning Opportunities with IRAs
- #10: Understand How GST Tax Exemption Impacts Planning

Case Study #1: Failing to Coordinate Asset Titling, Beneficiary Designations, TODs

Facts:

- Decedent is 80-year-old women survived by two sisters also in their 80s
- Will includes gifts to charities and remainder to sisters
- Sisters are named executors
- Sisters live out of state and out of the country
- Financial accounts are TOD to sisters

Case Study #1: Failing to Coordinate Asset Titling, Beneficiary Designations, TODs

- Issues:
  - Real estate is the only probate asset
  - No cash to pay expenses or make charitable gifts
  - Poor choice of fiduciary – being a family member alone is not a qualification!
  - What if sisters predecease?

Case Study #1: Failing to Coordinate Asset Titling, Beneficiary Designations, TODs

- Solution:
  - Simple revocable trust
  - Professional fiduciary
  - Coordination between financial advisor and lawyer
  - Takers in default clause

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Case Study #2: Failure to Obtain Holistic Advice

- Facts:
  - Husband has 4 adult children from first marriage and 2 minor children from second marriage (current spouse)
  - Husband makes will cutting out 1 adult son and leaving specific bequests to 3 other children from first marriage; residue to spouse
  - About 1 year prior to death, husband tells financial advisor that he wants to include his son again and will make a “TOD designation” on his investment accounts to the 4 adult children from his first marriage
  - Husband did not update his will after making TOD designations and later died

Case Study #2: Failure to Obtain Holistic Advice

- Issues:
  - After husband's death, wife received a very small percentage of his assets because the TOD investment accounts were paid to children from first marriage *in addition to* the specific bequests
  - Husband told financial advisor he presumed that the *later in time* TOD designation would satisfy the specific bequests to adult children under his will
  - Wife forced to file in court for elective share claim

Case Study #2: Failure to Obtain Holistic Advice

- Solution:
  - Thoughtful review of will provisions and TODs should occur whenever a TOD or beneficiary designation is changed
  - Consider that account values fluctuate over time and TOD and beneficiary designations are typically not the best solution unless all accounts are divided in accordance with the preferred percentages
  - Be mindful of default laws like elective share for a surviving spouse
  - Coordination between financial advisor and lawyer

Case Study #3: No Estate Plan & Challenging Assets

- Facts:
  - Decedent is a 60-year-old man survived by his wife and their minor child and his adult child from his first marriage
  - Decedent and wife have a “DIY” premarital agreement that is ambiguous
  - No will or trust
  - Decedent is a business owner with his brother
  - All assets are in the Decedent’s name, including primary residence

Case Study #3: No Estate Plan & Challenging Assets

- Issues:
  - Estate administration is delayed because of suit for aid and guidance regarding the premarital agreement to determine if the wife is a beneficiary of the estate
  - High administration expenses because of probate and valuation of business interests
  - Taxable estate
  - Conflicting interest between brother/business owner and family members
  - Wife has no cash to pay living expenses for herself and the minor child
  - No trust planning for minor child, so second suit filed for creation of trust for child
  - Trust for minor child will cause ongoing interaction with court system
  - High attorneys' fees because wife has a lawyer, estate has a lawyer, adult child has a lawyer, and minor child has a guardian ad litem

Case Study #3: No Estate Plan & Challenging Assets

- Solution:
  - Premarital agreement prepared by attorneys (each spouse should have separate representation)
  - Estate plan and business succession plan which avoids probate
  - Thoughtful review of joint ownership and TODs
  - Coordination between financial advisor and lawyer
  - Trust for minor child

Case Study #4: Confusing "Fair" with Equal

- Facts:
  - Husband and wife in their 70s want to prepare an estate plan leaving their assets to their adult children: child #1 is a successful corporate executive, child #2 is a recovered addict and financially dependent on clients
  - Clients want to leave more assets to child #2 because she "needs it"
  - Clients want to name child #1 as fiduciary
  - Estate plan includes mandatory distributions to child #2 upon surviving spouse's death

Case Study #4: Confusing "Fair" with Equal

- Issues:
  - Treating children unequally can cause strife between children after parents are gone
  - Allowing one child to be "in charge" of the inheritance of another child can create conflict
  - Potential change in circumstances→ child #2 relapses
  - Child #2 receives mandatory distributions that she cannot handle receiving
  - Child #1, as named fiduciary, files suit for custodial account for child #2's mandatory distributions so that the assets can be protected

Case Study #4: Confusing "Fair" with Equal

- Solution:
  - Gifting during lifetime; treating children equally under the will or revocable trust
  - Treat children unequally, but involve them in the estate planning process
  - Lifetime trusts with termination option by independent trustee
  - Professional fiduciary
  - Coordination between financial advisor and lawyer
  - Language in trust agreement regarding withholding of distributions due to beneficiary's unproductive activities, addiction, or bad health

Case Study #5: Declining Mental Capacity

- Facts:
  - Client is a 90-year-old man who you have worked with for 50+ years
  - Client is married to second wife and has two children from his first marriage
  - Will leaves primary residence to wife and all other assets to children
  - Client is starting to show signs of confusion about his assets and estate plan

Case Study #5: Declining Mental Capacity

- Issues:
  - Potentially losing mental capacity
  - Conflict between wife and children

Case Study #5: Declining Mental Capacity

- Solution:
  - Meet with whole family to review assets and estate plan (but understand waiver of privilege)
  - Document declining mental capacity
  - Coordination between financial advisor and lawyer

Case Study #6: Lost Will

- Facts:
  - Client is an elderly man with adult children from his first marriage; been happily married to second wife for 40+ years
  - Second wife also has adult children from her first marriage
  - Client signed a will 20 years ago leaving everything he owned to his wife, and took the original will home
  - Client and wife visited attorney shortly before client's death, and affirmed that their existing wills reflected their intentions to leave everything to the surviving spouse
  - Client did not want to set up a revocable trust and did not want to retitle/TOD assets because of cost, despite attorney's advice to set up revocable trust
  - Client died and wife couldn't find the original will

Case Study #6: Lost Will

- Issues:
  - Lost original will → need to petition court to admit copy of will to probate to allow all assets to pass to surviving spouse
  - Law presumes will was destroyed/revoked
  - Attorney who prepared will and witnesses who signed affidavit are all retired and out of state
  - Surviving spouse has burden of proving will was actually lost
  - If court rejects petition, assets will have passed by the laws of intestacy: 1/3 to surviving spouse and 2/3 to decedent's children from first marriage, leaving surviving spouse with insufficient assets

Case Study #6: Lost Will

- Solution:
  - Revocable trust would have avoided probate and court because typically a copy of a revocable trust is acceptable
  - Always keep track of original documents and notify spouse, children, advisors and attorneys of location
  - Consider allowing attorney to keep the original will (if attorney is willing to do so)
  - Don’t allow cost and time to be the primary factor driving decision-making
  - Coordination between financial advisor and lawyer

Case Study #7: Transfers of Assets Shortly Before Death

Facts:

- Client gets bad diagnosis and a short time to live
- Faced with an overwhelming situation, client, who despite having a solid relationship with an estate planning attorney, starts to make "DIY transfers" to children, upending the estate plan
- Client transferred business interests (commercial real estate LLC) to son even though client had made personal guarantees on the loans to the tune of $3M
- In transferring business to son, daughter is left out, but client's estate is on the hook for the personal guarantee on the loan
- Son can't afford to pay back estate for loan

Case Study #7: Transfers of Assets Shortly Before Death

Issues:

- This is surprisingly a common occurrence
- No gift tax return filed
- Transfer of the business assets subject to loan without lender approval triggered the "due on sale" clause
- Estate forced to quickly take out a loan for $2.5M to cover the loan because decedent personally guaranteed the loan
- The loan on the commercial real estate development was paid off, so the LLC now owned the property free and clear
- But LLC is owned 100% by the son because of pre-death transfer, and son only has ability to slowly repay dad's estate or must sell the building
- Daughter must wait many years, or potentially longer, to receive her inheritance, and estate still has obligation to repay its loan
- Also missed a step-up in income tax basis opportunity on the real estate LLC and business interests

Case Study #7: Transfers of Assets Shortly Before Death

Solution:

- Don’t make transfers without consulting attorney first!
- Often unknown ramifications such as tax planning, fairness, and “due on sale” clauses
- Depending on the outcome, could place intended beneficiaries in starkly different economic positions than realized
- Possible coercion or undue influence claims? Things can get messy, fast
- Plan ahead so quick decisions don’t need to be made -- and stick to the plan!

Case Study #8: Assuming the Conclusion

- Facts:
  - Clients are a married couple approaching retirement
  - Clients want to leave real estate to child #1, investment accounts to child #2, and life insurance to child #3 – it worked so well for their neighbor!
  - Clients want to name all three children as fiduciaries because they all plan to move back to Richmond
  - Clients are concerned about taxes

Case Study #8: Assuming the Conclusion

- Issues:
  - Clients are focused on specific assets not the big picture; asset values will change
  - Naming multiple fiduciaries can be a burden especially if they are out of state
  - What do the clients mean by “taxes”?
  - What if there are creditors?

Case Study #8: Assuming the Conclusion

- Solution:
  - Look at assets as a whole
  - Make equal distributions under revocable trust
  - Plan for today
  - Educate the clients
  - Coordination between financial advisor and lawyer

Case Study #9: Missed Planning Opportunities with IRAs

- Facts:
  - Client had an IRA that is a significant dollar value
  - Client created a thorough estate plan in 2019, including a see-through trust for his surviving spouse with discretion to distribute income and principal (not wishing to mandate distributions as she was his second wife), and separate see-through lifetime trusts for each of his adult children where all income and all retirement account distributions are distributed each year to the child (hoping to provide a steady income stream for each child)
  - Client's IRA beneficiary designations send his IRAs to the discretionary trust for his surviving spouse (or, to the lifetime trusts for his children, as the contingent beneficiary)
  - Client did not "dust off" his estate plan at the 3-year mark, as had been previously advised by his attorney, because he did not want to spend time or money to update his plan
  - Client dies in 2024, survived by his spouse and adult children

Case Study #9: Missed Planning Opportunities with IRAs

- Issues:
  - Client’s IRA will not receive “stretch” treatment, even though it is directed to a trust benefitting only his surviving spouse, because it does not qualify as a conduit trust
  - Client’s IRA will make distributions on an accelerated schedule, which also accelerates the income tax ramifications
  - If client had been predeceased by his surviving spouse, the all-income and all-retirement distribution trusts for his children would also have unintended consequences because the inherited IRAs would need to be liquidated within 10 years, and the “conduit” nature of the trust income payout would force the value of the IRA out and into the hands of the children within 10 years
  - The results would have been very different prior to the SECURE Act (eff. 2020) and proposed regulations issued in 2022, and SECURE Act 2.0 (eff. various)

Case Study #9: Missed Planning Opportunities with IRAs

- Solutions:
  - Frequent review of estate plan by a qualified advisor and attorney
  - Understand a detailed review of assets, documents, and new laws is necessary
  - Retirement account planning is an additional new burden requiring individualized analysis (no “one size fits all” advice)
  - Estate plan may need to be revised significantly to avoid retirement account landmines, although in the eye of the client the end result is largely “the same”
  - Financial advisor can identify when an update is needed, and urge client to take action with an attorney

Case Study #10: Understand How GST Tax Exemption Impacts Planning

- Facts:
  - Client created an ILIT many years ago (but after 2001) and made annual exclusion gifts each year
  - Client also created a zeroed-out GRAT after 2001
  - Client did not opt-out of automatic allocation of GST exemption to the ILIT or GRAT on a timely-filed gift tax return
  - Terms of the ILIT and GRAT make them an "indirect skip" and qualify the ILIT and GRAT as a "GST Trust"
  - Client did not otherwise ever make a taxable gift, and never used any of his lifetime gift tax exemption
  - In the "bonus exemption" year of 2024, client made a $13.61M cash transfer to a new irrevocable Dynasty Trust for the benefit of his children and grandchildren, and allocates all of his available gift and GST tax exemption to the transfer

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Case Study #10: Understand How GST Tax Exemption Impacts Planning

- Issue:
  - The client inadvertently used GST tax exemption for each annual exclusion gift to the ILIT, and the remainder of the GRAT
  - The client made a $13.61M gift to the 2024 irrevocable Dynasty Trust, but did not have $13.61M of GST tax exemption to allocate to the trust
  - The Dynasty Trust, which is intended to benefit the client’s grandchildren and possibly more remote descendants, now has a mixed inclusion ratio for GST tax purposes, which will trigger GST tax whenever a distribution is made to a grandchild or more remote descendant

Case Study #10: Understand How GST Tax Exemption Impacts Planning

- Solutions:
  - Proactive review of prior gifts and all prior gift tax returns *prior to making the gift to the Dynasty Trust*, would allow the client's advisors to recommend a better plan
  - Trustee of the Dynasty Trust may institute a "qualified severance" to separate the GST tax exempt assets from the non-exempt assets, and allow the GST tax exempt assets to grow without hindrance of GST tax on distributions to grandchildren
  - Depending on professional advice received by the client when the gift tax returns were filed to report the ILIT and GRAT gifts, the client may wish to seek a Private Letter Ruling from the IRS to undo the earlier automatic allocations
  - Other modifications or opportunities may be available

Questions?

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