HCR WEALTH ADVISORS

powered by The Clarity Formula®

February 23, 2023

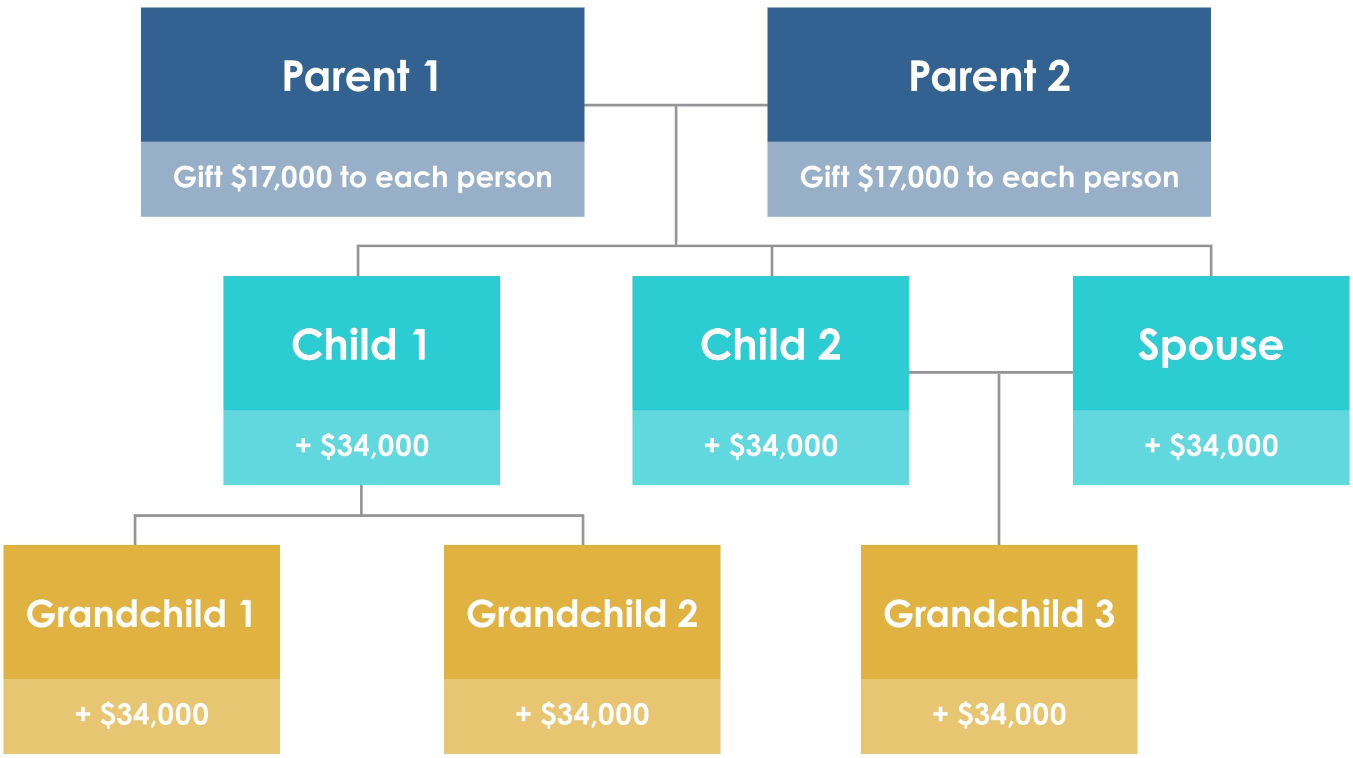
The Clarity Formula® – Estate Planning

The Tax Cuts and Jobs Act (TCJA) significantly increased the estate exclusion amount (presently $12.92 million for 2023). Under present federal legislation this limit is set to decrease to $5.0 million (adjusted for inflation) in 2026. With the increased gift and estate tax exemption amounts set to decrease in 2026, you may find yourself with the desire to reduce the size of your estate. There are three simple ways to reduce your estate that do not require an estate attorney.

Annual Gift Tax Exclusion

For 2023, the annual gift exclusion amount is $17,000 per donee, up from $16,000 in 2022. This means a donor can gift this amount to as many people as they want in 2023 without using any of their gift and estate tax exemption amounts or paying a gift tax. Married couples who elect to gift-split can give a combined $34,000 per donee without using any of their gift and estate tax exemption amounts or paying a gift tax. These gifts can go a long way in reducing the size of an estate and producing significant estate tax savings.

The illustration below outlines how a married couple with children and grandchildren can transfer $328,000 tax free to reduce the size of their total estate.



Tuition Payments Made Directly To An Educational Institution

Tuition payments made directly to a college do not count as gifts for gift tax purposes. This allows parents, grandparents, and other individuals to reduce their taxable estate by helping to cover the cost of college for a child. Additionally, these direct payments do not count toward annual gift tax exclusion amount. One drawback for making direct tuition payments is the potential impact on financial aid. Typically, a tuition payment made directly a college will reduce a student's eligibility for needs based financial aid.

Payments Made Directly To A Healthcare Provider

Payments made directly to a medical institution or care provider for the benefit of an individual do not count as gifts for gift tax purposes. This allows for parents, grandparents or other individuals to reduce their taxable estate by covering medical expenses for loved ones or other individuals. Additionally, these direct payments do not count toward the annual gift tax exclusion amount. The expenses that qualify are the same as those that are deductible for income tax purposes.

Over the past year, we have all felt the effects of inflation, mostly in a negative way. However, the federal estate exemption saw a significant increase year over year thanks in large part to inflation. This allows for additional gifting opportunities for those who may have already exhausted their lifetime amounts. The chart below highlights the annual changes to many of the federal estate planning limits.

Federal Estate Planning Limits

	2021	2022
Estate Exclusion	$12,060,000	$12,920,000
Maximum Estate Tax Rate	40%	40%
Lifetime Gifting Exemption	$12,060,000	$12,920,000
Maximum Gift Tax Rate	40%	40%
Annual Gift Exclusion	$16,000	$17,000
Annual Gifting Limit to U.S. Citizen Spouse	Unlimited	Unlimited
Annual Gifting Limit to Non-U.S. Citizen Spouse[1]	$164,000	$175,000

Estate planning is very specific to each individual or family and their unique situation and desires. There is no one size fits all approach. Different estates will require different documents and vehicles to best distribute assets in accordance with the wishes of the deceased. The "Guide to Estate Planning" below will give you a brief highlight and help you familiarize yourself with many of the components of an estate plan.

Level One (Must Haves)

Planning for and documenting the transfer of assets with minimized tax and transfer cost. Review upon life events (marriage, divorce, birth, adoption, etc.)

- A **will** appoints guardians for you children and spells out specifically how you want your property split.
- A **Living Trust** avoids probate, allows for privacy, and designates how assets are to be divided upon your death.
- A **Healthcare Power of Attorney** allows you to designate a Healthcare agent to make healthcare decisions in the event you are unable to make decisions for yourself.
- A **Financial / Property Power of Attorney** allows you to designate an agent to make financial decisions in the event you are unable to make decisions for yourself.
- Joint accounts transfer to a designated person upon death, it is important to **review co-ownership provisions and the titling of accounts.**
- Some assets (such as IRAs, Life Insurance, and Annuities) pass to your designated Beneficiaries. **It is very important to periodically review beneficiary designations and coordinate with the overall estate plan.**

Level Two (Considerations)

Further enhance the direction of assets, minimize Estate Taxes or increase Asset Protection

- The **Spousal Lifetime Access Trust (SLAT)** has become a popular estate planning strategy to take advantage of current lifetime gift tax exemptions ($12.06MM each).
- **Grantor Retained Annuity Trusts (GRAT)** seek to pass assets to beneficiaries free of estate and gift tax that have appreciated over the IRS Section 7520 interest rate.
- Explore Charitable Trust, Donor-Advised Fund and Foundation Options.
- Since Life Insurance is not necessarily estate tax-free, consider establishing an **Irrevocable Life Insurance Trust.**
- Qualified Personal Residence Trust (QPRT)
- **Intra-Family Loans** can provide family members lower borrowing rates than traditional financing options.
- **Special Needs Trusts** ensure the proper passing of assets to ensure beneficiaries with special needs are not disqualified from entitled benefits.

Level Three (Advanced)

For Complex Estate Tax Issues or Liability Concerns

- **Domestic and Offshore Asset Protection Trusts** offer those in high liability fields of work and those with high estate tax brackets options to reduce liability.
- **Self-Cancelling Notes** allow the exchange of property for periodic payments based upon mortality.
- **Family Limited Partnerships and Family LLC's** provide legal, financial, and tax structure to family businesses.

Concept Check: Portability

Portability allows you to use you spouse's unused estate tax exclusion. While portability was made permanent for federal estate tax purposes, you should check if your resident state also allows for portability of a deceased spouse's unused estate exclusion. In the event your resident state does not allow for portability, it may make sense for both spouses to have assets in their respective name (or trust's name) up to the resident state's estate exclusion amount. Note that portability may require the filing of estate tax returns at first death even if there is not a taxable estate.

Estate planning can alleviate stress for you and your loved ones by helping to protect your legacy in the manner you desire, provide for your dependents and heirs, replace uncertainty with confidence and allow your loved ones to focus on grieving and healing.

If you have any questions that pertain to your specific situation, please do not hesitate to your advisor.

Sources: JDSURPA, Saving for College, The Balance