The Importance of Estate Planning in Ever-Changing Times

This is a series in which Rochester Rotary explains the importance of having your estate documents completed and regularly reviewed, especially in the changeable environment in which we live. Part I outlined why estate plans are important for everyone. Part II provides the specific elements of a good estate plan. Our final installment discusses why estate plans can be a hedge against the changes we'll all experience in the future.

If you would like to learn more about transferring assets in ways that can benefit the Sunshine Camp, please contact Heather Rossi, Development Director, at heather@rochesterrotary.org.

Part III: Estate Plans in Ever-Changing Times

If we've learned nothing else over the last three years, it's that life changes, and it now changes at an alarmingly fast rate. Some of the issues that will impact you and your family in the future and can have profound implications for financial well-being include:

- Income law changes
- Estate tax changes
- Social Security benefit modifications
- Capital gains rules changes
- Retirement plan rule changes
- Increasing stock market volatility
- Inheritance and gifting rule changes

Over the next two decades, more than $30 trillion in wealth is going to be transferred from the current asset owners to heirs or charitable organizations. Anyone between 45 and 85 years old is part of that great wealth transfer, and a ripple effect will exist for generations.

Regardless of your net worth, estate planning includes determining the method of asset transfers that are most beneficial for the people that give the assets and the people and organizations that receive them. Let's consider a few of the most important factors:

Tax Implications

Tax implications are a key factor when determining how and when to transfer assets. It's important to understand whether the asset is taxable when you draw money from it, or when you transfer it to heirs.

Generally speaking, if an asset was funded or purchased with pre-tax dollars (like your employer retirement funds or traditional IRAs), then all money taken out of it is taxed at the time of withdrawal. If the asset was funded with after-tax dollars (like a Roth IRA), then money withdrawn is tax-free. These tax rules also apply to heirs who receive these assets: be aware that if you intend to transfer assets to your children or other heirs like an employer retirement plan or traditional IRA, you will transfer the taxes due on those funds as well.

Part of the estate planning process includes an assessment of the best assets to use for individual heirs vs. charitable giving.

Estate Values, Taxes, and Transfers

In recent years, debates about the taxable values of estates have heated up. Generally, when you die, your estate is not subject to the federal estate tax if the value of your estate is less than the exemption amount. In 2023, the exemption amount is $12.92 million for an individual, and a combined exemption of $25.84 million for a married couple. For New York State estate tax purposes, the individual exemption is $6.58 million for an individual and a combined exemption of $13.16 million for a married couple.

Only a small percentage of Americans at the highest wealth levels die with an estate worth $12.92 million or more. On the other hand, estates in the range of $5 million to $10 million are not uncommon; small business owners and corporate managers often realize wealth that creates estates with those values, and New York State estate tax rates must be considered.*

Estate planning includes asset allocation strategies that protect some of your estate value from taxes, and creates a method of asset transfer that avoids passing taxes to heirs. This includes determining if you have the opportunity to plan for transferring assets to individual and charitable beneficiaries outside of an estate, such as:

- Designating a beneficiary in your retirement funds
    - Consider designating a charitable beneficiary for taxable funds such as employer retirement funds or traditional IRAs as a charity would not pay the tax an heir would upon disbursement
    - Accounts such as Roth IRAs are not taxable funds and would not leave implications for heirs.
- Making qualified charitable distributions from your retirement plan to reduce your required minimum distribution that would otherwise be taxable
- Creating a charitable lead trust or a charitable remainder trust to benefit both charitable and individual beneficiaries
- Invest in a charitable gift annuity to provide lifetime fixed income to yourself while leaving the remainder to charity after your death.
- Purchasing a permanent life insurance policy and naming beneficiaries
- Some investments can be Transfer on Death assets
- Joint asset with rights of survivorship allow for a spouse or partner to receive the assets without them passing through the decedent's estate.

Transferring assets outside your estate may lower the total amount of your taxable estate and can help avoid estate taxes.

Timing – Transfer Now or Bequeath Later?

Planning determines whether a transfer of money now is better than inheriting. You should consider whether an inheritance will happen too late for the beneficiary to benefit? Do your beneficiaries need the cash now more than later? Do YOU need access to the cash or asset because you don't know if your future financial needs will be met? And will an inheritance create a tax event for your beneficiaries? Will a gift given now have tax implications?

Right now, one person can give any one person up to $17,000 in a year and generally not have to deal with the IRS about it. If you give more than $17,000 in cash or assets (includes a car or other tangible asset) in a year to any one person, you need to file a gift tax return. This is simply a disclosure, not tax on the gift. However the excess may reduce any exemption available to the donor at the subsequent death of the donor. The recipient does not need to claim the gift as income.

You can give up to $17,000/year to multiple people, and multiple people can give up to $17,000/year to the same person. So, for example:

Aunt Becky wants to help her 4 nieces/nephews. She starts a 529 for each with $5,000 per. Next year, she puts $20,000 into each account. She's now triggered a tax disclosure and the excess may affect her available exemption after death.

Grandfather and Grandmother add $30,000 to each 529. No disclosure is required because it is treated as a $15,000 gift from each of them as long as it came from two different accounts. When Grandfather and Grandmother add $50,000 to each 529, they've now exceeded the amount to avoid a disclosure, and the excess may affect their available exemption at death.

The gift tax disclosure allows the IRS to keep track of your excess gifts over your lifetime to see whether or not your estate tax exemption should be reduced.

As you can see, the methods and implications of asset transfer can become complicated, and the rules change year-over-year. As your asset mix changes, it becomes more complex. It behooves you to have an advisor create a well-thought-out plan that addresses these issues.

This series is not intended to be tax, legal or investment advice and is provided for general educational purposes only. You should consult with your tax and legal advisor regarding your individual situation.

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** Current federal estate tax rates would require that most of an estate's value is taxed at a 40% rate. For New York State estate tax purposes, estates in excess of 105% of the exemption amount would be fully taxed based on the entire value of the net estate, at rates ranging from 3.06% to 16%. For estates in excess of the exemption amount but less than 105% of the exemption amount, only the excess is taxed.*

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