



## ESTATE PLANNING

Estate planning is the process of arranging the management and disposal of a person's estate during their life and after their death, while minimizing gift, estate, generation-skipping transfer, and income tax. Estate planning involves the bequest of assets to heirs and the settlement of estate taxes.

### Powers of Attorney

A power of attorney (POA) is a legal document that grants one person (known as the "agent" or "attorney-in-fact") the authority to act on behalf of another person (known as the "principal") in specific matters. The scope of this authority can be broad or limited, and it can be temporary or enduring, depending on the type of power of attorney established. The authority granted under a power of attorney terminates upon the death of the principal. There are several types of powers of attorney, each serving different purposes.

**General Power of Attorney:** This gives the agent broad powers to handle the principal's financial and legal affairs, such as managing bank accounts, real estate, and other assets, signing documents, and entering into contracts. A power of attorney may end if the principal becomes incapacitated, or may be durable, meaning it remains in effect upon incapacity.

**Special or Limited Power of Attorney:** This grants the agent authority to act on the principal's behalf in specific situations only. For example, a person might create a special power of attorney to allow another person to sell a car or a house.

A power of attorney may be effective immediately upon execution, or may be springing. A springing power of attorney becomes effective only under circumstances defined in the document, typically when the principal becomes incapacitated. This allows the principal to keep control over their affairs until a specific triggering event occurs.

It's important to note that the agent has a fiduciary duty to act in the best interests of the principal. The power of attorney should be drafted carefully to ensure that it accurately reflects the principal's wishes and provides the necessary protections. While most powers of attorney may provide a general grant of authority, it is important to note that there are some powers that are considered so personal in nature to the principal that they are not permitted unless specifically authorized under the terms of the document.

### Advanced Medical Directives

An advance medical directive, also known as an advance healthcare directive, consists of two separate documents usually contained in a single document. The first is a **medical power of attorney** that gives the agent the authority to make healthcare decisions on the principal's behalf if the principal becomes incapacitated and unable to make such decisions. The other is a **living will**, which outlines a person's preferences regarding medical treatments and interventions in the event that they become unable to communicate their decisions due to illness or incapacitation. The living will component typically covers decisions about:

**Life-Sustaining Treatment:** Whether or not the individual wants treatments that could extend their life in situations where recovery is unlikely, such as mechanical ventilation, resuscitation (CPR), artificial nutrition and hydration, and dialysis.

**Pain Management and Comfort Care:** Preferences regarding palliative care, which focuses on relieving symptoms and improving quality of life, rather than attempting to cure an illness.

**Organ and Tissue Donation:** Whether the individual wishes to donate organs and tissues after death.

**End-of-Life Wishes:** Specific instructions regarding the individual's care at the end of life, including where they would like to spend their final days (e.g., at home or in a hospital), and any religious or spiritual rituals they would like observed.

## Wills

A will, formally known as a "Last Will and Testament," is a legal document that expresses a person's wishes as to how their property is to be distributed after their death and as to which person (the executor) is to manage the property until its final distribution. Key aspects of a will include:

**Asset Distribution:** The primary function of a will is to outline how the individual's assets—such as money, property, and personal belongings—should be divided and who should receive them. These recipients are known as beneficiaries. Wills often include contingency plans in case the primary beneficiaries are unable to inherit. This can include secondary beneficiaries or instructions for how the assets should be distributed if the primary beneficiaries predecease the testator.

**Executor Appointment:** The will names an executor (also known as a personal representative), who is responsible for carrying out the wishes expressed in the will, managing the estate, settling debts, and distributing assets to the beneficiaries.

**Guardianship:** For individuals with minor children or dependents, a will is used to appoint guardians who will take responsibility for their care if the parent or guardian dies before the children reach adulthood.

**Instructions for Debts and Taxes:** The will can provide instructions for how debts, expenses, and taxes should be paid, and from which assets.

For a will to be legally valid, it must comply with the laws of the state in which it was created. This typically involves the will being written, signed, and witnessed according to the state's requirements. In Virginia, unless the Will is wholly in the decedent's handwriting, referred to as a holographic will, a will must be signed by a testator in the presence of at least two competent witnesses who are present at the same time. It is recommended that the witnesses be "disinterested," meaning they are not beneficiaries of the will, to avoid potential conflicts of interest. To avoid having to locate the witnesses upon the death of the testator, most wills include a sworn statement, which is notarized, by the testator and the witnesses that affirms they were present and that they believed the testator was of sound mind and acting voluntarily.

If a person dies without a valid will, they are said to have died "intestate," and their assets will be distributed according to state law, which might not align with their wishes.

## Trusts

Trusts are legal arrangements in which one party, known as the trustor or grantor, gives another party, the trustee, the right to hold title to property or assets for the benefit of a third party, the beneficiaries. Trusts are established to provide legal protection for the grantor's assets, to ensure those assets are distributed according to the grantor's wishes, and to save time, reduce paperwork, and in some cases, avoid or reduce inheritance or estate taxes.

Unlike wills, trusts are effective immediately, and as a result, are tools that provide for the management of assets both during life and upon the grantor's death. Trusts can be arranged in many ways and can specify exactly how and when the assets pass to the beneficiaries. They come in various types, each serving different needs and purposes. Here are some common types of trusts:

- **Revocable Trust (Living Trust):** This trust allows the trustor to retain control over the assets during their lifetime and is flexible, meaning it can be altered or revoked at any time. Upon the grantor's death, the assets pass to the beneficiaries according to the terms of the trust. These trusts may divide into subtypes upon the grantor's death. Common subtypes include:
  - **Marital Trust:** Designed to provide benefits to a surviving spouse; generally included in the taxable estate of the surviving spouse.
  - **Credit Shelter Trust (Bypass Trust):** Allows both spouses to take full advantage of their estate tax exemptions, passing assets on to heirs free of estate tax.
  - **Descendants Separate Trusts:** Manage and protect assets for the benefit of the grantor's children, grandchildren, or further descendants.
- **Irrevocable Trust:** Once established, this trust cannot be altered or revoked by the trustor. The assets placed into the trust are permanently removed from the trustor's estate and transferred to the trust. This type of trust can have tax benefits and asset protection benefits.
- **Testamentary Trust:** This trust is created as part of a will and comes into effect upon the trustor's death. It details how the trustor's assets will be distributed after they pass away.

- **Charitable Trust:** Established to benefit a particular charity or the public in general. A charitable trust can offer tax benefits for the trustor while supporting a cause they care about.
- **Special Needs Trust:** Designed to benefit individuals with disabilities by managing assets for their benefit without disqualifying them from receiving government assistance.
- **Spendthrift Trust:** Protects the beneficiary's inheritance from creditors or from the beneficiary's own spending habits by only distributing assets according to the terms set by the trustor.
- **Life Insurance Trust:** Holds a life insurance policy within the trust, allowing the trustor to exclude the life insurance proceeds from their taxable estate.
- **Asset Protection Trust:** Designed to protect the grantor's assets from creditors. These are often established in favorable jurisdictions and are irrevocable for a specific period.
- **Medicaid Planning Trusts:** Designed to help individuals who might otherwise be over the asset limit to become eligible for Medicaid, particularly for long-term care coverage, which can be very expensive.

Trusts are complex legal tools that can involve intricate tax rules and regulations. They require careful drafting and a clear understanding of the grantor's objectives.

## Other Methods of Asset Transfers

Not all assets are controlled under the terms of a will or trust. Such assets are usually types of property and assets that do not go through the administrative process of an estate or trust, and pass directly to a designated beneficiary directly upon an individual's death. Such assets include:

**Jointly Owned Property with Right of Survivorship:** Property that is owned jointly with the right of survivorship (such as a house owned by a married couple) will automatically pass to the surviving owner without going through probate. This could include a variety of assets, such as a financial account, vehicle, or real estate.

**Payable-on-Death (POD) or Transfer-on-Death (TOD) Accounts:** Bank accounts, life insurance policies, brokerage accounts, retirement accounts, and other financial accounts with designated beneficiaries will transfer directly to those beneficiaries upon the account holder's death. Some retirement accounts may have default provisions for determining a beneficiary in the absence of a beneficiary designation.

**Transfer on Death Deed:** This legal document allows property owners to name one or more beneficiaries to inherit real estate upon their death. This tool is recognized in some but not all U.S. states and provides a simple way to transfer property upon death.

**Life Estate Deed:** The owner of real property may transfer property to a remainderman, while retaining the right to occupy and use the property for the duration of their life. The life tenant is responsible for paying property taxes, insurance, and maintaining the property in good condition. The remainderman receives full ownership of the property upon the death of the life tenant, or upon some other event disqualifying event, but does not have the right to use or receive income from the property until the life tenant passes away.

It's important to regularly review and update beneficiary designations for nonprobate assets to ensure they align with current wishes and estate planning goals. In many cases, the designations for these assets will take precedence over instructions left in a will, so keeping them current is crucial for the intended distribution of the estate.

## Taxes

When an individual passes away, their estate may be subject to various taxes, depending on the value of the estate, the location, and the laws in effect at the time of death. Such taxes may include:

**Estate Taxes (Federal and/or State):** Estate taxes are levied on the transfer of the "taxable estate" of a deceased person. The federal estate tax is imposed on estates exceeding a certain exemption threshold, which is adjusted periodically for inflation. Some states have their own estate taxes with different exemption thresholds and rates.

**Probate taxes:** Probate taxes are fees assessed by a court or government authority for the legal process of administering and settling an estate after someone's death. The term "probate tax" might be used informally to refer to these costs, but it's not a tax in the traditional sense. Instead, these are the fees associated with the probate process. Probate taxes vary widely depending on the jurisdiction and the size of the estate.

**Inheritance Taxes:** Unlike estate taxes, which are paid out of the estate itself, inheritance taxes are paid by the individual beneficiaries of an estate. Not all states impose an inheritance tax, and the rate can vary

depending on the beneficiary's relationship to the decedent (for example, spouses are often exempt, while distant relatives or non-relatives may pay a higher rate).

**Income Taxes:** The estate is responsible for filing a final income tax return for the deceased person, covering the period from January 1st of the year of death up to the date of death. Additionally, if an estate or trust generates income during the administration period (for example, through investments or rental property), it may be subject to income taxes as a separate entity, requiring the filing of an estate income tax return, known as Form 1041.

**Capital Gains Taxes:** Beneficiaries may be subject to capital gains taxes if they sell inherited assets, particularly if the assets have appreciated in value since the date of the original owner's death. However, beneficiaries often receive a "step-up in basis," which means the cost basis of the asset is adjusted to its fair market value at the time of the original owner's death, potentially reducing the capital gains tax owed.

**Property Taxes:** Real estate within the estate may continue to accrue property taxes until it is transferred to the beneficiaries or sold.

**Gift Taxes:** If the deceased person made significant gifts before death, there might be implications for gift taxes, although there are annual and lifetime exemptions for gifts as well.

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