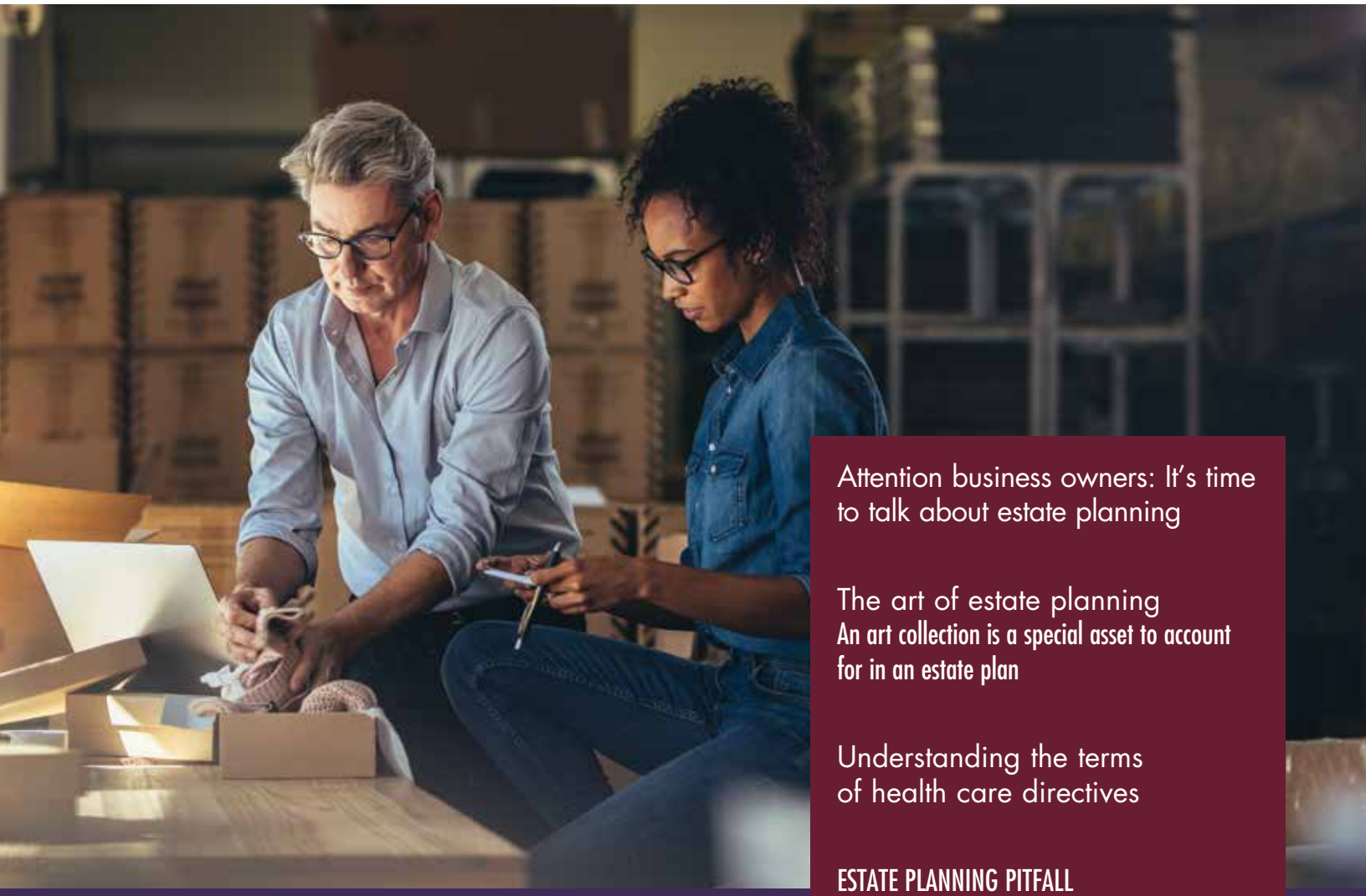
INSIGHT ON ESTATE PLANNING



FEBRUARY / MARCH 2021

STOKES LAWRENCE

Seattle | Yakima

Stokes Lawrence | 1420 Fifth Avenue, Suite 3000 | Seattle, Washington 98101-2393 | 206.626.6000

Stokes Lawrence Velikanje Moore & Shore | 120 N. Naches Avenue | Yakima, Washington 98901-2757 | 509.853.3000

www.stokeslaw.com

Attention business owners: It's time to talk about estate planning

If you're a small business owner, you probably don't have a minute to spare in your busy workday, especially if you're struggling to recover after a turbulent 2020. Estate planning may be one of the last things on your mind.

However, not only can estate planning help ensure that your objectives are met should you die unexpectedly or become disabled, it may also protect the business you've spent years building. Also, if it suits your purposes, an estate plan can provide a smooth transition to the next generation.

Start with the basics

As with most individuals, a comprehensive estate plan should be supported by a core of several key documents. For starters, a basic will divides up your assets among designated beneficiaries, including your business interests, as well as meeting other objectives. Without a will or having assets otherwise titled, your business and other assets will be distributed under the prevailing laws in your state, regardless of your wishes.

In addition, adopt a power of attorney for someone to manage your affairs in the event you become incapacitated. This "attorney-in-fact" can conduct business transactions. The power of attorney should be complemented by health care directives providing guidance if you can't make medical decisions for yourself. (See "Understanding the terms of health care directives" on page 5.)

Customize your estate plan to accommodate your business needs. For instance, in some states a spouse won't be able to access business assets without court approval. To avoid this result, you might place assets in a trust you've established as legal owner.

Terms of a buy-sell agreement

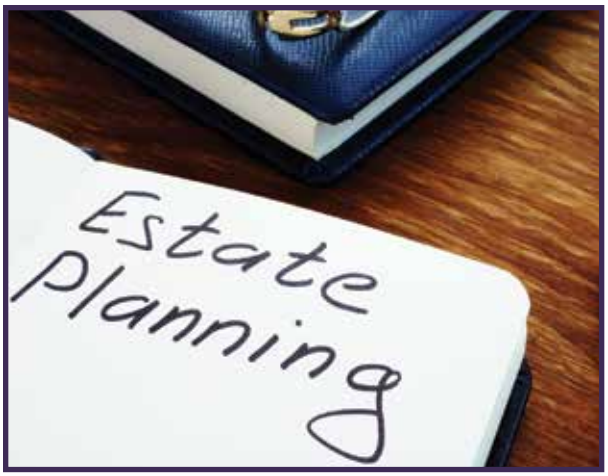
Do you own a business with one or more co-owners or partners? A buy-sell agreement may avoid legal complications when a co-owner or partner passes away or is disabled.

A buy-sell agreement establishes who can buy a business, the main terms of the agreement and the basis for determining a price. For instance, with a cross-purchase agreement, a surviving owner is entitled to make the purchase. An entity-purchase agreement provides the means for selling your interest back to the company.

Typically, a buy-sell agreement is funded with life insurance on the lives of the owners and partners.

Consider tax implications

If you own significant business assets, consider maximizing the federal estate tax breaks currently on the books. This includes the use of the unlimited marital deduction and the generous federal gift and estate tax exemption. For 2021, the exemption shields assets valued up to $11.7 million.



Be aware that certain states also impose their own state or inheritance tax. Note that inheritance tax paid by family members such as your children comes out of their own pockets — not the estate's.

Fortunately, you can minimize taxes on both the federal and state levels by using multiple trusts or setting up a family limited partnership (FLP). With a tax-favored FLP, the assets are removed from your taxable estate. Finally, be aware of tax consequences for ultimate distributions of retirement plan accounts to designated beneficiaries.

Succeed through a succession plan

In many cases, a business owner's fondest dream may be to transfer ownership to his or her children, who will continue to run the operation when the owner retires. A succession plan can provide a smooth transition of power and be used in the event of an unexpected death of an owner.

Typically, a succession plan will outline the structure of the business going forward and prepare for the eventual sale of the business. Make sure that the plan is memorialized in writing. Identify training opportunities and special compensation arrangements for your successors. One section of the plan should include all the financial details reflecting assets, liabilities and current value.

Coordinate your succession plan document with your will and the other estate planning documents discussed above.

Resolve sensitive family issues

It's not unusual for a family to face internal challenges and struggles as the entrepreneur reaches retirement age. Unfortunately, leaving one sibling out in the cold while another is anointed to run the business can create hard feelings. Or giving someone a secondary role may cause conflicts.

One common estate planning strategy is to attempt to "even things out." For example, say for simplicity that you own a business valued at $5 million and you have $5 million in other assets. You have named one of two children to succeed you as the business owner. In this case, you can give the successor child the $5 million in business assets and leave the remaining $5 million in assets to the other child.

You can minimize taxes on both the federal and state levels by using multiple trusts or setting up a family limited partnership.

Of course, you may run into other intrafamily squabbles. And don't forget to factor your extended family — such as the spouses of your children — into the equation.

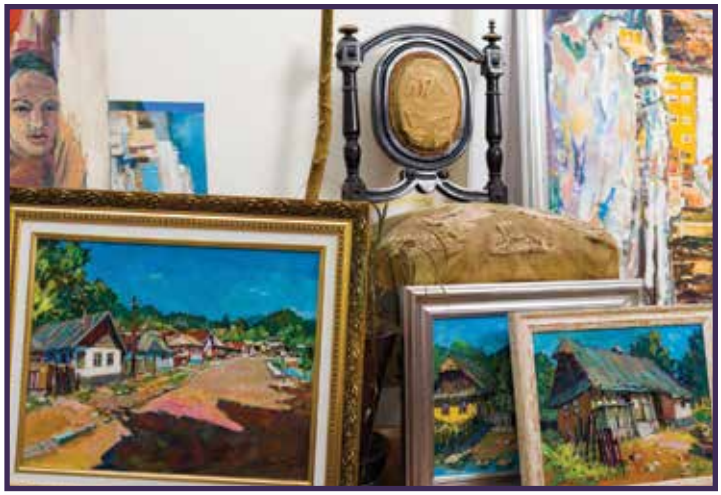
Final words

Now is the time to get potential issues out into the open. Have a frank discussion with the parties who will be affected. Your estate planning advisor can help shape a plan to meet your unique circumstances as a business owner. •

The art of estate planning

An art collection is a special asset to account for in an estate plan

It goes without saying that your art collection, including paintings, sculptures and other pieces of art, can represent a significant portion of your estate. Thus, it's critical to account for these assets in your estate plan.



While you can apply many traditional estate planning strategies to an art collection, this asset type can present unique challenges. Of course, you'll want to preserve the value of your collection and avoid unnecessary taxes but knowing how your collection will be managed and displayed after your death may also be of importance.

What's the collection worth?

It's vitally important to have your collection appraised periodically by a professional. The frequency depends in part on the type of art you collect, but generally it's advisable to obtain an appraisal at least every three years, if not annually.

Regular appraisals give you an idea of how the collection is growing in value and help you anticipate tax consequences down the road. Also, most art donations, gifts or bequests require a "qualified appraisal" by a "qualified appraiser" for tax purposes.

In addition, catalog and photograph your collection and gather all appraisals, bills of sale, insurance policies and other provenance documents. These items will be necessary for the recipient or recipients of your collection to carry out your wishes.

What are my options?

Generally, there are three options for handling your art collection in your estate plan: Sell it, bequest it to your loved ones, or donate it to a museum or charity. Let's take a closer look at each option:

1. If you opt to sell, keep in mind that capital gains on artwork and other "collectibles" are taxed at a top rate of 28%, compared to 20% for other types of assets. Rather than selling the collection during your lifetime, it may be preferable to include it in your estate to take advantage of the stepped-up basis, which allows your heirs to reduce or even eliminate the 28% tax. For example, you might leave the collection to a trust and instruct the trustee to sell it and invest or distribute the proceeds for the benefit of your loved ones.

2. If you prefer to keep your collection in the family, you may opt to leave it to your heirs. You could make specific bequests of individual artworks to various family members, but there are no guarantees that the recipients will keep the pieces and treat them properly. A better

approach may be to leave the collection to a trust, LLC or other entity — with detailed instructions on its care and handling — and appoint a qualified trustee or manager to oversee maintenance and display of the collection and make sale and purchasing decisions.

3. Donating your collection can be an effective way to avoid capital gains and estate taxes and to ensure that your collection becomes part of your legacy. It also entitles you or your estate to claim a charitable tax deduction. To achieve these goals, however, the process must be handled carefully. For example, to maximize the charitable deduction, the artwork must be donated to a *public* charity — such as a museum or university with that status — rather than a private foundation. And the recipient's use of the artwork must be related to its tax-exempt purpose. In other words, the recipient would have to exhibit it or use it for art education, for example, rather than selling it. Also, if you wish to place any conditions on the donation — such as specifying where the collection can or cannot be displayed or including your name on signage accompanying the artworks — you'll need to negotiate the terms with the recipient before you deliver the items.

If you plan to leave your collection to loved ones or donate it to charity, it's critical to discuss your plans with the intended recipients. If your family isn't interested in receiving or managing your collection or if your charitable beneficiary has no use for it, it's best to learn of this during your lifetime so you have an opportunity to make alternative arrangements.

The right strategy for you

The greatest value of a piece of art may be intangible, but that doesn't lessen the need to properly account for it in your estate plan. With careful planning and qualified valuation assistance, it can create significant tax benefits. Qualified valuation and estate planning advisors can design a strategy that's right for you. •

Understanding the terms of health care directives

Estate planning experts usually cite the need to include advance health care directives in a comprehensive estate plan. But there's often disagreement about the legal names given to those directives and their optimal use, depending on one's jurisdiction.

In any event, regardless of what they're called in the state where you reside, it's important to create these documents and keep your family in the loop. Let's take a closer look at a few health care directives.

Health care power of attorney

Comparable to a durable power of attorney that gives an "agent" authority to handle your financial affairs if you're incapacitated, a health care power of attorney (or medical power of attorney) enables another person to make health care decisions for you. This is also called a health care proxy in some states.

Choosing an agent is critical. You probably can't anticipate every situation that might arise — virtually no one can — in which it's likely that someone will have to make decisions concerning your health. Therefore, the agent should be a person who knows you well and understands your general outlook. Frequently, this is a family member, close friend or trusted professional.

Remember to designate an alternative and successor in the event your first choice is unable to do the job.

Living wills

A living will is a legal document that establishes criteria for prolonging or ending medical treatment. It indicates the types of medical treatment you want, or do not want, in the event you suffer from a terminal illness or are incapacitated.

This document doesn't take effect unless you're incapacitated. Typically, a physician must certify that you're suffering from a terminal illness or that you're permanently unconscious. Address common end-of-life decisions in your living will. This may require consultations with a physician.

The requirements for living wills vary from state to state. Have an attorney who's experienced in these matters prepare your living will based on the prevailing laws.

DNRs and DNIs

Despite the common perception, it's not a legal requirement for you to have an advance directive or living will on file to implement a "do not resuscitate" (DNR) or "do not intubate" (DNI) order. To establish a DNR or DNI order, discuss your preferences with your physician and have him or her prepare the paperwork. The order is then placed in your medical file.

In fact, even if you already have a living will spelling out your preferences regarding resuscitation and intubation, it's still a good idea to create DNR or DNI orders when you're admitted to a new hospital or health care facility. This can avoid confusion during emotionally charged times.

POLSTs

Finally, in some states, an estate plan may include a document known as a "physician order for life-sustaining treatment" (POLST) or a similar name. A POLST may be used by a person who has already been diagnosed with a serious illness.

This document doesn't replace your other directives. Instead, it complements other directives to ensure you receive the treatment you prefer in case of an emergency. Your physician completes the form based on your instructions and personal conversations.

The POLST is posted by your bedside if you're hospitalized. If you're residing at a health care facility, it should be prominently displayed where medical or emergency personnel can easily view it.

Putting directives into action

Advance directives must be put in writing. Each state has different forms and requirements for creating these legal documents. Depending on where you live, you may need to have certain forms signed by a witness or notarized. If you're unsure of the requirements or the process, contact an attorney for assistance.

Review your advance directives with your physician and your health care agent to be sure you've accurately filled out the forms. Then let all the interested parties — including your attorney, physician, power of attorney agent and family members — know where the documents are located and how to access them.

Revise as needed

Finally, be aware that advance directives aren't written in stone. You can revise them at any time. Just be sure to follow your state's requirements for revisions. Contact your estate planning advisor and attorney with questions. •

ESTATE PLANNING PITFALL

Your elderly relative won't commit to estate planning

There are many obstacles in the path to estate planning. One of the more difficult to overcome is when an elderly parent or family member refuses to cooperate or even acknowledge the need for estate planning measures. And this could lead to problems — such as family feuds and potential financial disasters — down the road.

Depending on their health status and other factors, including finances, your parents may resist your efforts to assist them in basic estate planning. Short of taking matters to court to have an elderly relative declared incompetent — generally, a last resort — develop a plan that provides some basic estate planning components. This will require a heart-to-heart talk with the relative.

The first thing to do, and perhaps the most important, is to initiate a family meeting. (Because of the ongoing COVID-19 pandemic, the meeting may have to take place online.) Invite all the key players — your parents, siblings and, as appropriate, their spouses, at the least — to the gathering.

What should you discuss? Cover the entire estate planning gamut. This isn't the time to be evasive — the dialogue should be frank and honest. Many issues can be sensitive and emotions can run high, so be prepared for some hand-wringing or pushback.

You probably won't be able to accomplish all your objectives in a single session. Consider meeting again with as many of the other parties as possible. In fact, you might broaden the circle to include your professional estate planner. Take as much time as you need to work things out.

STOKES LAWRENCE

Seattle | Yakima

Stokes Lawrence, P.S.
1420 5th Avenue, Suite 3000
Seattle, Washington 98101-2393
206.626.6000

Stokes Lawrence
Velikanje Moore & Shore
120 N. Naches Avenue
Yakima, Washington 98901-2757
509.853.3000

www.stokeslaw.com

Estate Planning During a Pandemic

As the COVID-19 pandemic continues into 2021, it is natural to think about getting your affairs in order, if only to be better safe than sorry. Making sure you have a Will, and an up to date one at that, is always a good idea, but can provide additional peace of mind at a time like this.

At the same time, the circumstances of a pandemic make it uniquely challenging to take care of your estate planning needs. Under normal circumstances, an attorney and client would meet in person at least once, if not several times, in order to prepare final documents. Most documents also require either witnesses or notarization. The most common estate planning document, a Last Will and Testament, requires two witnesses. For a number of reasons, it is best that these witnesses are not beneficiaries named under the Will. Unfortunately, this makes it difficult to use family members, who may be housemates, as witnesses.

All these concerns and the potential for financial stress during a pandemic might leave a person considering an online fill-in-the-blank style Will. While this may seem like a good idea to accomplish your estate planning needs, or at least to act as a stopgap until after the pandemic, for a number of reasons utilizing a form Will is a bad idea. For instance, people using these Wills often fail to make a residuary bequest which is a catch all provision that distributes the portion of the estate not specifically bequested to other beneficiaries. Failing to include a residuary bequest can result in an estate passing to unintended beneficiaries and, at worst, passing to a person the drafter intended to disinherit. Additionally, proper and thorough drafting helps to prevent later challenges to the Will. The legal fees associated with such challenges can quickly diminish the value left to be distributed to intended beneficiaries. Finally, consulting with an attorney helps to ensure that the legal formalities of Will execution are met and that any appointments to fiduciary roles take into consideration the limits to who may serve.

If you need to take care of your estate planning, even in a pandemic it is still best to consult an attorney. Up until execution of the final documents, the entire process can be done telephonically and with video conferencing equipment. Execution of the documents will require witnesses and notarization, but your attorney should be able to provide witnesses in a safe and socially distanced environment. Your attorney or another service may also be able to provide remote notarization so that being in the physical presence of the notary is not required.

If you are interested in putting together an estate plan, or updating your current estate plan, please contact a member of the Stokes Lawrence Estate Planning Group at (206) 626-6000 in Seattle or (509) 853-3000 in Yakima.