Should You Do It Yourself?

LegalZoom™ advertises itself as a cheaper alternative to an attorney. Intuit, through its "Quicken WillMaker™", and other do-it-yourself programs, entice people to forgo professional advice, assuring them that the documents they create will be "just as good as one created by an attorney."

These programs and web sites are popular with lawyers, too! Why? Because they make more work for lawyers in the future.

Recently, *Consumer Reports* magazine recently evaluated LegalZoom, Nolo, and Rocket Lawyer in an article "Legal DIY sites no match for a Pro" (September 2012, p. 13.) The editors concluded that unless your needs are very simple, the will writing products of these companies not only are unlikely to meet your needs, but can even lead to unintended results. Among other issues, too often the documents produced are not properly tailored to individual jurisdictions (states). As stated in the article, "Many consumers are better off consulting a lawyer."

Laws are not static. They constantly change because of new case law and statutes. And lawyers keep up with these changes in order to best advise their clients. That's why these online legal sites issue significant disclaimers. For example, on the top left-hand corner of its estate planning questionnaire, LegalZoom reveals that 80 percent of people who fill in blank forms to create legal documents do so incorrectly. Despite this disclaimer, LegalZoom tries to reassure its customers that professionals are there to help; that customers can have "peace of mind" knowing that LegalZoom professionals will customize their will based on their legal decisions.

The hard fact is that people who use do-it-yourself estate planning kits end up with a false sense of security. They create documents that they believe will address their estate

planning needs. But with estate planning documents, they are unlikely to discover their mistakes.

Why? Because the mistakes will not become evident until after they become incapacitated or die. And the people who will be left to deal with the mistakes are usually the people the documents were supposed to protect.

Attorneys don't simply fill in forms. Rather, we use the knowledge we have acquired during our many years of schooling and practice to advise you on the best way to protect your family, and preserve and distribute your assets in the manner you choose. And yes, that has a price.

Judge Orders Refund to Estate That Paid Tax Before Madoff Con Was Revealed

When New Jersey resident Theodore Warshaw died in 2006, his estate was valued at more than $1.8 million. Because in New Jersey any amounts in an estate above $675,000 are subject to estate tax, Mr. Warshaw's executors paid $88,677 to the state.

The bulk of Mr. Warshaw's assets were held in an IRA, and when he died the IRA went to a trust to benefit his widow. The IRA assets were allegedly being invested in stocks, bonds and other financial instruments by Bernard L. Madoff Securities, LLC. Mr. Madoff's company reported that at the time of Mr. Warshaw's death the value of the IRA was more than $1.4 million.

In December 2008, Mr. Madoff was arrested and it was revealed

that Mr. Warshaw was among the victims of the largest Ponzi scheme in U.S. history. The money in Mr. Warshaw's IRA was not being invested but instead had been used to pay other "investors." The IRA's value was not $1.4 million but $0.

Learning this, Mr. Warshaw's estate requested a refund of the $88,677 estate tax it had paid New Jersey. The estate argued that the IRA actually had no value at the time of Mr. Warshaw's death and that therefore his taxable estate was well below the state's $675,000 threshold. New Jersey's Division of Taxation denied the requested refund.

Both sides asked the Tax Court of New Jersey to rule in their favor without a trial. In its argument to the court, the state Division of Taxation cited a 1929 U.S. Supreme Court holding that the value of assets in a taxable estate cannot be determined by events after the date of a death. *Ithaca Trust Co. v. United States*, 279 U.S. 151.

On June 28, 2012, the Tax Court of New Jersey ruled that the Division owes Mr. Washaw's estate the refund. The court wrote that despite the 1929 Supreme Court ruling, "subsequent events may be considered to establish evidence of fair market value as it existed on the date of death." The court held that the discovery of the Madoff Ponzi scheme was relevant to the determination of the IRA's value at the time of Mr. Warshaw's death, and that the IRA was in fact worthless at that time.

To read the tax court's decision in the case, *Estate of Warshaw v. Director, Division of Taxation,* click here.

Should You Give It Away?

For wealthy individuals and couples, gifting has always been an important part of estate planning. And now that the gift tax exemption stands at $5 million (5.12 million adjusted for inflation in 2012) and the top gift tax rate is 35%, the tax environment is especially favorable for making large gifts. Gifts of up to $5.12 million ($10.24 million for couples) in 2012 incur no gift tax. BUT – these levels are scheduled to expire after 2012, with the exemption automatically shrinking to $1 million and the top tax rate jumping to 55% on January 1. So – should you take advantage now? If you do, are there any pitfalls? .

1. If you think Congress will act before next January 1 to make the $5 million exemption and 35% tax rate permanent, there's no pressure to act (and I've got a bridge I'd like to sell you).
2. On the other hand, if you expect Congress to allow the estate tax to revert to 2001 levels – a $1M exemption and 55% top tax rate – you should seriously consider a gifting strategy – but you should be aware of a potential pitfalls.

First, the advantages. If you can afford to give up some or all of the benefit of the gifted property, it will remove from your estate all of the appreciation on and income from the property and avoid state estate taxes in states, such as Maryland, where there is no state gift tax.

Second, the pitfalls. Your donees will loss the benefit of the "step up" capital gains basis (although this will not be a problem if the asset already has a high basis), and gifts will still be included in your federal taxable estate and subject to the unlikely, but possible "clawback" tax, a scenario in which you might lose the benefit of the $5.12 million exemption.

To understand the "clawback" issue you should know how the estate tax actually is calculated (optional reading for the mascohistic):

Example 1. Assume a man is unmarried and owns assets worth $6 million, and makes a gift of $5 million in 2012, fully shielded by his $5 million exemption. He then dies, also in 2012, owning the remaining $1 million. When the trust or estate attorney prepares his federal estate tax return, the 2012 taxable gift of $5 million must be added back into the taxable estate at the date-of-gift value for purposes of calculating the estate tax amount. (Yes, it doesn't make sense. Write your Congressperson.) Thus the full $6 million would be included in the man's taxable federal estate, but would be offset by full use of his $5 million estate tax exemption[1]. This is done so that the remaining $1 million is "bumped" into a higher estate bracket, if there are higher brackets at the time of death. As long as the estate tax exemption available at death ($5 million in this example) is at least the same as the gift tax exemption used during life (also $5 million in this example), however, only the $1 million would be taxed.

In this example, the only advantage to making the gift is that any future appreciation in the gifted asset's value is shielded from gift and estate taxes, although there may be a capital gains income tax disadvantage because of loss of the "stepped up" basis to the donee of the gift.

Example 2. Now assume the gift and estate tax exemptions are $5 million in 2012, as in Example 1. Also assume future legislation establishes the exemption at $3.5 million after 2012, keeping the estate tax rate at 35% (a legitimate possibility if Congress finally gets its act together next year). Assume you own $6 million and in 2012 you gift $5 million to your adult children, fully shielded by your 2012 exemption. You die in 2013, owning the remaining $1 million.

Following the methodology described above in Example 1, to calculate your estate tax, you must include the gifted $5 million in your estate tax calculation, and then make full use of your estate tax exemption, which we have assumed to have decreased to $3.5 million. The result is to expose to the 35% estate tax not only your remaining $1 million, but also another $1.5 million (i.e., the decrease in exemption from $5 million to $3.5 million). The result could be an estate tax of $875,000 on an estate of $1 million. If the estate tax rate in 2013 is assumed to be 45%, the result could be an estate tax of $1,125,000 on an estate of $1 million – and Internal Revenue Service might try to collect $125,000 from the gift recipients!

This result is the "recapture problem" or "Clawback." Important – despite the Clawback, making the gift does NOT incur any additional tax. The estate ultimately receives just the benefit of the applicable exclusion amount at the individual's death if the Clawback applies. But liquidity certainly is an issue in this example – how will the estate tax will get paid, and which beneficiaries will bear the cost

Will Clawback happen?

Probably not, at least according to most tax experts, who contend that the Clawback interpretation is flawed. Many point to the obvious public policy concerns raised by such a tax – it obviously is unfair for taxpayers to make gifts in reliance on the current tax law and later be subject to tax because those laws change, and it is "likely not what Congress intended."[2]

But if Clawback happens . . .

If Clawback happens, the donor's estate still is likely to have benefited from the gifts made in 2012. The Clawback would be at the amount of the taxable gift, not the current value of the property given away. Therefore, the appreciation

on the property given will not be taxed.[3] If the gift had not been made, the amount of the gift plus appreciation would be subject to tax. In a large estate, this can be significant.

In summary . . .

On balance, taking advantage of a $5 million exclusion that likely will disappear in 2013 is a great opportunity, and it is recommended for large estates with high basis assets that are likely to substantially appreciate. But – as always, a cost-benefit analysis should be made of the risk and timing of the gift, and the loss of control in the assets.

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[1]Technically it's not an exemption, but a credit equivalent. However, it is more understandable to refer to it as an exemption.
[2]Am. Bar Ass'n, Estate and Gift Tax Comm., *Tax Relief, Unemployment Reauthorization, and Job Creation Act of 2010 27 (2011)*
[3]But this must be balanced against the loss of the "stepped up" basis of the assets that would be available if the assets passed at death.

Can You Execute?

Being the "Personal Representative" or "PR" of an estate – the modern term for executor – is not a task to take lightly. The Personal Representative is responsible for managing the administration of a deceased individual's estate. Although

the time and effort involved will vary with the size of the estate, even if you are the executor of a small estate you will have important duties that must be performed correctly or you may be liable to the estate or the beneficiaries.

How do you become a Personal Representative? The PR is either named in the will or if there is no will, appointed by the court. You do not have to accept the position, even if you are named in the will.

The average estate administration takes six months to one year, although small estates typically can be resolved in a few months. Following are some of the duties you may have to perform as executor:

- **Locate documents**. If there is a will, but you don't already know where the will is or the will hasn't already been brought to court, you may need to find it among the deceased's belongings. If all you have is a copy of the will, you may need to get the original from the lawyer who drafted it. You will also need to get a copy of the death certificate.
- **Hire an attorney**. You are not required to hire an attorney, but mistakes can cost you money. You may be personally liable if something goes wrong with the estate or the payment of taxes. An attorney can help you make sure all the proper steps are taken and deadlines met.
- **Apply for probate**. If there is a will, the court will grant you "letters testamentary" If there is no will, you will receive letters of administration (although in some states, like Maryland, letters of administration are used in both cases.) This will officially begin your work as the executor.
- **Notify interested parties**. Notify the beneficiaries of the will, if there is a will, as well as any potential heirs (such as children, siblings, or parents who may or may not be named in a will). In addition, you will have

to place an advertisement for potential creditors in a newspaper near where the deceased lived.

- **Manage the deceased's property**. You will need to prepare a list of the deceased's assets and liabilities, and you may need to collect any property in the hands of other people. One of the executor's jobs is to protect the property from loss, so you will need to assure the property is kept safe. You will also need to hire an appraiser to find out how much any property is worth. In addition, if the estate includes a business, you may have to make sure the business continues to run.
- **Pay valid claims by creditors**. Once the creditors are determined, you will need to pay the deceased's debts from the estate's funds. The executor is not personally liable for deceased's debts. The estate usually pays any reasonable funeral expenses first. Other debts include probate and administration fees and taxes as well as any valid claims filed by creditors.
- **File tax returns**. You need to make sure the tax forms are filed within the time frame set under the law. Taxes will include estate taxes and income taxes.
- **Distribute the assets to the beneficiaries**. Once the creditors' claims are clear, the executor is responsible for making sure the beneficiaries get what they are entitled to under the will or under the law, if there is no will. You may be required to sell property in order to fulfill legacies in a will. In addition, you may have to set up any trusts required by the will.
- **Keep accurate records**. It is very important to keep accurate records of everything you do. You will need to create a final accounting, which the beneficiaries must review before the distribution of the estate can be finalized. The accounting should include any distributions and expenses as well as any income earned by the estate since the deceased died.
- **File the final accounting with the court**. Once the final accounting is approved by the beneficiaries and the

court, the court will close the estate. File a final report with the court and close the estate.

All this can be a lot of work, but remember that the executor is entitled to compensation, subject to approval by the court. Keep in mind that the compensation is counted as income, so you will need to declare it on your income taxes.

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Disinheriting A Relative

You may feel that you have given one child more during your life, so he or she should get less in your will. Or you may want to cut out an heir altogether. Whatever the reason, disinheriting a close relative—especially a spouse or a child—can be complicated.

It generally is not possible to completely disinherit a spouse. Even if you don't leave your spouse anything in your will, most states have laws that keep a spouse from losing everything – usually the spouse is entitled to one-half or one-third, depending upon whether you have children. If you live in a "community property" state, your spouse already owns half the community property. Also, the definition of your "estate" varies from state to state; in some states it includes only your probate estate and not trusts, retirement accounts, life insurance or other assets. In some states, all or part of these "non probate" assets are included in the spouse's share.

Even if you don't completely disinherit your spouse, he or she can choose between taking what the will provides or taking what the law in your state says a spouse should receive in any

case (the “statutory share,” usually one-third to one-half of the estate). The only solution is to enter into an agreement with your spouse in which you each waive the right to receive anything from the other’s estate.

Disinheriting a child is a different story. You will need to check with an attorney in your state to find out what is required. Louisiana is the only state that does not allow an adult child to be disinherited. While other states do not require that you leave anything to your adult children, there may be laws that protect minor children. For example, in Florida you are required to leave your house to either your spouse or a minor child, if they are living. In addition, there are often laws that protect children born after a will was written. To be safe, even if you are leaving a child nothing, you should specifically mention the child in the will. It may also help to state the reason the child is getting nothing or a reduced amount. If you don’t mention a child at all, the state may conclude that you did not intentionally exclude the child.

Disinheriting a close relative can cause fights among family members. Squabbles over wills can drag on for years and prevent your heirs from receiving their inheritance, so if you are planning on disinheriting someone, it is important to take as many precautions as possible and consult with an elder law or estate planning attorney.

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