

Post-Death “Planning” Can Be Better Than You Think

The term “planning” generally implies action taken before an event occurs to ensure that what happens after the event flows smoothly. Ideally, estate planning provides the opportunity to make prudent decisions before death -- on both a tax and a personal level. Sometimes, however, pre-death planning is not possible. Fortunately, several post-death strategies are available.

Qualified Disclaimers

If Mom never gets around to changing her will, and on her death leaves her entire \$3 million estate to Dad, the children may ultimately suffer a tax loss of approximately \$250,000. Within nine months of Mom’s death, however, Dad can disclaim his right to receive \$625,000 (the unified credit exemption equivalent for 1998, rising to \$1 million by 2006), allowing this amount to pass tax-free to the children. As long as Dad doesn’t need those funds, this technique makes a lot of sense.

QTIP Elections

A standard estate plan provides that on the death of the first spouse, assets equaling the exemption equivalent pass to a credit shelter trust, which will not be included in the survivor’s estate. The balance passes to the surviving spouse, generally in trust. If the trust is designed as a qualified terminable interest property (QTIP) trust, the executor must elect to allow the trust to qualify for the marital deduction, which will defer the tax on the trust assets until the survivor’s death. Total deferral, however, is not always desirable. Making a partial QTIP election so that some tax is paid on the first death may result in a lower overall tax burden.

The Executor’s Role

The elections that the executor can and must make after your death have far-reaching impact. The executor ultimately bears the responsibility for becoming familiar with tax law and estate planning issues, working with the family and its advisors, and making the best elections given the circumstances. An executor’s actions can have significant tax savings and expense implications. For example, when the second spouse dies shortly after the first spouse, the overall tax burden may be higher if the executor has elected full QTIP on the first spouse’s death. Why? Paying some tax on the first death may allow the combined estates to take advantage of lower tax brackets.

Hindsight Is 20/20

Post-death planning presents additional opportunities because better decisions may be made when all the circumstances are known. The old maxim, hindsight is 20/20, holds true.

Post-Death Planning for Business Owners Section 6166 Estate Tax Deferral

Under certain circumstances, estates holding a qualifying closely held business interest can pay estate taxes in installments, over a period as long as 14 years. If your estate qualifies for this deferral, it receives preferred interest rate. Sounds great, doesn’t it? Well, deciding to pay estate tax in installments has several drawbacks:

1. Deferral means being saddled with the tax burden for 14 years.
2. The interest paid in the installments is no longer deductible for estate tax purposes, while interest paid on a traditional loan may still be deductible.
3. Choosing to qualify for 6166 limits your ability to dispose of the qualifying business interest for the duration of the “loan.”
4. Premature disposition will result in tax acceleration. Again, this does not occur with a traditional loan.

FOBI Exclusion

The Taxpayer Relief Act of 1997 introduced an exclusion for qualified family-owned business interests (FOBI). The new exclusion may be taken to the extent that the exclusion for FOBI, plus the amount effectively exempted by the unified credit, does not exceed \$1.3 million. A qualified FOBI is any interest in a trade or business with a principal place of business in the United States and ownership of at least 50% held by one family, 70% held by two families or 90% held by three families, and at least 30% held by the decedent's family. Not only will it be difficult to meet these qualifications, but if you do, the election may still not be worthwhile. Analysis of the numbers and the family's long-range business will be required.

Alternate Valuation Date

If estate tax liability will decrease, the estate can value the assets six months after the decedent's death -- the alternate valuation date. While this election seems simple enough, the impact of choosing an alternate valuation date can be significant. Among other things, the chosen date can affect the ability to benefit from the 6166 election, the FOBI exclusion and special-use valuation. Like 6166, the business can only pass to qualified heirs and must stay within the family for at least 10 years. If disposition occurs too soon, the benefits of the exclusion are subject to recapture.