

## Estate Planning and Intergenerational Transfer of Land

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### What is estate planning?

- ▣ Accumulation, management, conservation, and transfer of wealth based on
  - The law
  - The taxes
  - What you want to have happen...
- ▣ Because death is inevitable...
- ▣ We want to understand what makes an effective and efficient transfer
  - Get it transferred to correct person/persons/entity(ies) in best manner possible with minimal cost

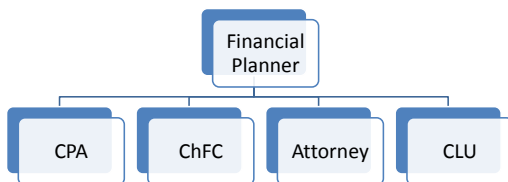
## Estate Settlement Process

1. Initial responsibilities (funeral, etc.)
2. Probating Will
3. Appointment of executor or administrator
4. Assembling estate property
5. Managing estate
6. Payment of debts and taxes
7. Distributing estate

### So goals and objectives of estate planning are:

- ▣ Efficient and effective transfers
- ▣ Meet client's wishes for property transfers
- ▣ Minimize taxes associated with transfer
  - Income taxes
  - Gift taxes
  - Generation skipping tax
  - Estate tax
  - State inheritance tax – Note: Florida lost its estate tax after 2004 because of the change in the federal system made a tax credit previously used into a deduction at the federal level. This in effect wiped out Florida's tax which had been based on the credit.

### The Players



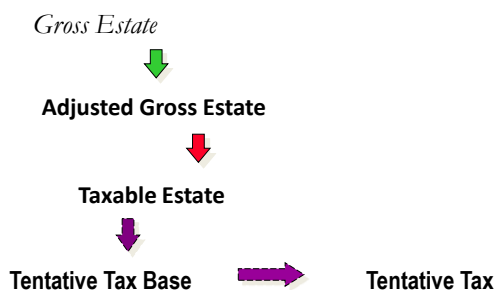
- Minimize transfer costs
  - Lawyer's fees
  - CPA fees
  - Documents' fees
  - Court fees
  - Taxes
- Maximize net distributions to heirs
- Provide for liquidity needs at death
- Fulfill health care wishes

## Planning barriers (personal)

- Facing one's own mortality or that of a loved one
- General procrastination...
- No health concerns
- Cost
- Ignorance
- Not aware of their estate's value...
- Who needs an estate plan?
  - Single with no dependents?
  - Married?
  - People with children?
- What if people don't plan?
  - Who get's grandma's yellow pie plate?

## Importance of Estate Planning

- Asset Disposition
  - Do things go to whom you want?
  - Do things get used for what you want them to be used for?
- What are examples where this is not the case...
- Maximize financial efficiency of transfers
  - Minimize taxes



## Deductions from Adjusted Gross Estate

- Marital Deduction
  - Unlimited
  - Tax-Free
  - Property included in decedent's gross estate
  - Actually passes to spouse
- Charitable Deduction
  - Qualified charities only
  - 100% deductible
  - Simple

## *Tentative Tax Base*

Taxable Estate

+

Adjusted Taxable Gifts

(all post-1976 taxable gifts decedent made during lifetime that are not included in gross estate)

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## Tentative Tax Calculation

- Current estate tax is extended indefinitely, which would otherwise expire at the end of the year
- 45% is permanent for estates over \$3.5 million for singles and \$7 million for couples
- If Congress takes no action by December 31, then spring 2011 is back to 55% for estates over \$1 million

## Credits

- Gift tax payable
  - Any gift paid out-of-pocket on gifts in 3 years is included
  - Decedent gets a credit for all gift taxes paid during lifetime
  - Taxable gifts are added back to taxable estate, up to \$1 million
- Applicable Credit Amount
  - \$1,455,800 (\$3.5 million exclusion)
  - $\rightarrow \$1,500,000 * 45\% = \$555,800 +$
  - $\rightarrow \$2,000,000 * 45\% = \$900,000$
  - $\rightarrow$  ZERO Estate Tax Owed

## Gift Example

- Estate is worth \$3.5 million, made a \$1,000,000 gift
 

Taxable Estate	\$3,500,000	
Plus Gift	\$1,000,000	
	\$4,500,000	
	First \$1,500,000	\$555,800
+	Next \$3,000,000 (*45%)	<u>\$1,350,000</u>
		\$1,905,800
-	Less Applicable Credit	\$1,455,800
	Net Estate Tax DUE	<u>\$450,000</u>

What is the lesson?

Get appreciating assets out of the estate!  
Gifts can elevated the estate tax bracket

## Generation Skipping Transfer Tax

- A beneficiary (related person) who is at least two generations younger than the transferor
- \$13,000 annual exclusion per donee for lifetime direct skip transfers
- Same as federal flat rate 45%
- Not included in “gross-up” rule, like gift taxes
- Transferor is liable for GSTT on direct skips

## Probate Transfers

- Probate is the process used by state judicial supervision to make an orderly distribution of property, claims by creditors and will publication of a decedent to the beneficiaries
- Assets subject to probate:
  - Single entity – owned assets
  - Tenancy in Common (simultaneous multi-owner) property
  - Community property
  - Any asset(s) designated to beneficiary as “estate of insured”

## Non-Probate Assets

- Life Insurance
- JTWRROS / Entirety
- Gift taxes paid in last 3 years
- General powers
  - Entitles holder to transfer property, subject to the estate, creditors to the holder and the estate
  - Classified as “special” or “general” depending on the conditions of exercisability
    - “Limited” time period or specific circumstances

## Tax Avoidance Strategies

- Inter-vivos (among the living) revocable trusts
  - Most grantors name themselves trustee
  - At death, the trust becomes irrevocable
    - Continues at a later date OR
    - Terminates with the corpus distributed
  - Potentially lower costs than probate, may avoid completely
  - Alternative to guardianship/conservatorship
  - Greater privacy and speed of disposal of property

## Land Easement Trusts

- Section 2031(c) of Internal Revenue Code allows beneficiaries to exclude up to 40% of the otherwise taxable land subject to a qualifying conservation easement
- Limited to \$500,000
- Can be done post-mortem by heirs, prior to filing estate taxes (9 months typically)
- Property anywhere in the US is eligible
- Must be donated to a public charity
- Easement must protect outdoor recreation, education resources, wildlife habitat, or open space for the “scenic enjoyment of the general public or in fulfillment of a clearly delineated public conservation policy”
- Historic are treated differently under section 170(h)

## Land Easements

**Example 1: Estate Tax Savings**

Value of land before easement	\$1,000,000
Value of land after easement (remainder value)	\$700,000
Value of easement	\$300,000

**Calculation of Exclusion**

Remainder value	\$700,000
Exclusion percentage	40%
Amount of exclusion (remainder times exclusion %)	\$280,000

**Calculation of Tax Savings**

Value of exclusion	\$280,000
Savings due to exclusion (\$200,000 taxed at 49%)	\$137,200
Value of easement	\$300,000
Assumed estate tax rate 49%	
Savings due to reduction in value	
(\$300,000 taxed at 49%)	\$ 147,000
<b>Total Estate Tax Savings due to Easement</b>	<b>\$284,200</b>

**Tax Savings as Percent of Donation\* 94.7%**

\*In other words, the tax saving achieved was 94.7% of the value given up through the donation.

## The PAPERWORK

- Wills
- Side letters of instruction
- Power of Attorney (PoA) : Property
- Durable PoA for Healthcare
- Living Will or Advance Medical Directives
- DNR

## Estate Settlement Process

- Intestacy
  - Death without a valid Will
  - State laws determine how estate is distributed to heirs
  - Are they in line with your wishes?
    - [http://www.mystatewill.com/statutes/fl\\_law.htm](http://www.mystatewill.com/statutes/fl_law.htm)
      - FL LAWS
    - [http://www.mystatewill.com/degrees\\_of\\_kinship.htm](http://www.mystatewill.com/degrees_of_kinship.htm)
      - Kinship Chart
    - <http://www.mystatewill.com/states/FL/FLintcalc.htm>
      - Intestacy Calculator

## Avoidable outcomes

- Not What Dad Wanted
  - [Ties to your land](#)
- A Tale of Two Sons
  - [Ties to your land](#)
- Deathbed Planning
  - [Ties to your land](#)

## Communicating with family

- Initiating the conversation can be difficult
  - Topics of money and our own mortality can be very uncomfortable to discuss
  - Deciding who gets what
  - What to do with assets
    - Pass on to loved ones (inheritance)
    - Sell
    - Conserve Land

## When it comes to land, not either/or situation

- “Many owners are torn between not wanting to see their land developed and wanting to provide an inheritance for children or other heirs. However, it does not have to be an “either/or” situation. Creative planning and compromise can allow for some measure of both. The key is to open the lines of communication so the planning process can begin. “

## 3 reasons why you should start now:

- A. If you should die unexpectedly without a plan, either the State, your heirs, or both will create one for you. Their plan may not look much like your plan.
- B. You may lose significant income, tax benefits, or both, by waiting to protect land using a last will and testament. Good planning can save land now, save or earn you money now, and may save your heirs money later.
- C. Peace of mind. If you keep thinking about this, you must want to do it. Taking steps to protect your assets changes your worry into pride and contentment.

## Heirloom Scale of Valuation

\$ \_\_\_\_\_ 😊  
1                      5                      10

**1 = Financial Asset in Our Portfolio**

**10 = Priceless Heirloom to Family**

- Where are you today? Where are your spouse and children?
  - Generally, people move towards priceless along this scale over time.

## When should I start planning?

- **NOW!**
  - Protecting family assets (including land) is not an issue you want to put off until just before you die.
  - It takes significant professional time to execute!!!
  - Remember, your estate plan “ensures that your wishes are carried out with a minimum of inconvenience and expense to your family.”

## Land Owner #1

- Small Landowner Scenario (125 acre parcel)

## Land Owner #2

- Large Landowner scenario (1000 acre parcel)

## Life Insurance

- Can be used to:
  - Build up an estate
  - Cover estate settlement costs
  - Preserve the farm business
  - Pay decedents debts
  - Fund passage of farm to certain children while providing an equal amount of cash to nonfarm heirs
  - Provide income for surviving spouse

### Not what Dad wanted (video example)

- Son worked on farm with Dad every day
- Three daughters moved away and married well
  - Had no interest in the farm
- Estate split evenly between siblings
- Son did not have enough money to buy the sisters' portion of the farm
  - He ended up driving a truck for a living instead of doing what Dad wanted him to do – take over the farm

### Same scenario – this time Dad has Life Insurance and a Will

- How would Dad's planning affect the situation?

### Same scenario – this time Dad has Life Insurance and a Will (cont.)

- His wishes would be in writing
  - There would be less arguing over what Dad actually wanted
- The son could have the farm and the sisters could each receive their share of the estate via the life insurance benefit (cash)
- Avoid probate court and all the accompanied stress and fees during a time of grief

### Worksheet: Starting the Planning Process

- Determining what you want to accomplish with transfer
  - Keep in family
  - Keep in conservation if family is not interested
  - Sell

## Worksheet: Starting the Planning Process

- Determining what you want to accomplish with transfer
  - Keep in family?
  - Keep in conservation?
- What is fair in the context of your family?
  - Not everyone necessarily needs or is interested in the same thing
- Distribution options/consequences

## Resources

- Who Gets Grandma's Yellow Pie Plate ? Workbook 1999 University of Minnesota
- Who Will Get Grandpa's Farm? (<http://www.ces.purdue.edu/farmtransfer/index.htm>)
- Money Talk – A financial guide for women
- Ties to the Land – TiestotheLand.org
- Iowa State University Extension – Estate Planning Publication PM 993 (2006)

## Additional Questions?

Local extension office or  
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