Episode #316 - 3 P's of Estate Planning

Hi and welcome back to this week's episode of Money Script Monday. My name is Laurence Williams. Today we'll be talking about the 3P's in estate planning. When most people envision estate planning, they often imagine affluent individuals packed in boardrooms, consulting with financial experts, lawyers and Cpas. But today, I wanted to dispel the notion that estate planning is exclusively for the wealthy.

Regardless of your financial standing, crafting an estate plan is a crucial step in securing your legacy and ensuring a smooth transition of your assets to your loved ones. Estate planning, simply put, is determining how an individual's assets will be preserved, managed, and distributed after death or in the event that they become incapacitated. Everyone tuning in today has an estate. Today we'll be reviewing the following: What are some of the 2024 estate planning opportunities? What are the 3P's of estate planning and what are some considerations to make when planning for your estate?

First, let's review the 2024 state planning opportunities. Who owes the state taxes? Every individual has their own lifetime unified credit exemption, allowing them to pass a specified amount tax free to anyone during their lifetime or at death. There are some exceptions, such as unlimited marital deductions, which allows married couples to transfer assets to each other without using their exemption. Additionally, there's an annual gift exclusion which allows individuals to give a set amount to as many people as they wish without affecting their exemption. For 2024, the annual exclusion is $18,000.

Married couples can also combine their exemption through a process of electing portability on their estate tax return, allowing their surviving spouse to potentially double their exemption. The estate tax rate itself varies depending on your taxable estate’s value, starting at 18%, reaching all the way to 40% for those amounts exceeding $1,000,000. But truth be told, many households will continue not to have an estate tax issue after the sunset with $7,000,000 in exemption instead of the $13.61 million, which is a significant decrease. Looking at historical trends, it will still impact around 1% of households per year.

However, for our high-net-worth individuals 2024 and 2025 presents estate planning opportunities to leverage the expanded exemption before that window closes. The IRS has indicated that there are no penalties for individuals using their expanded exemption before sunset, really making it a “use it or lose it” situation. By making strategic moves like gifting assets or establishing specific trusts, individuals can shield significant assets from future estate taxes.

For individuals with the liquidity to do so, taking advantage of the expanded exemption could save almost $3,000,000 in future estate taxes, which is the difference between the 2024 exemption and the projected post sunset exemption of $7,000,000 times that 45% estate tax rate. Or perhaps there's individuals on a rapid increase in their net worth, maybe through their own business, making good investments or those high-income earners. Look at your financial outlook now and run a scenario analysis to see if some certain estate plan moves makes sense today.

Now let's take a look at the three P's of estate planning. There are two initial primary considerations when it comes to estate planning, which are property and people. First two P's. With property, in order to pass your property to the people you want to receive it, you first must know what you have. There are several ways to get a handle on your property and calculate your gross to state. One of those is by updating your financial statement semi-annually. If you own real estate or investments, you know those values can fluctuate rapidly for better or for worse. An updated financial statement will give you an accurate picture of your property and investment values as well as your debt.

Also take physical inventory. Your tangible personal properties, jewelries, collectibles, and vehicles. Will either have cash value or sentimental value to someone when you pass, but probably both and an inventory will help make it easier for your heirs to identify the property and whom it's intended for at a difficult time. Once you've identified what you possess, you now must consider who you want to receive your estate, or at least part of your estate when you die, which takes us to the second P, which is people.

Now these are not always easy decisions to make, particularly when it comes down to possessions that have deep and personal meetings for you. But to help people you care about receive what you want them to, having a will or a trust in place will really do two things for your heirs. It can, one, help you avoid probate. Without wills and trusts, your estate may have to go through a process called probate, which will make the financial affairs public, delay your heirs from receiving their inheritance, and cost them potentially a small fortune in attorney fees.

It can also help you avoid any family conflict specifying who gets what in the form the name beneficiaries reduces the probability of discord between your family members. This means your property and assets will be distributed accordingly to your wishes, not whatever family member gets there first. So now that you've considered the first two P’s, property, and people, you now must consider the third one, which is protection. Your property and your people in your life need to be protected against a few risks, namely taxes and income tax, federal and estate tax, along with the big one, which is lifestyle damage.

This is where life insurance can be a tremendous tool in your overall estate plan because life insurance prevents these enemies from really gaining foothold. After you've completed your estate plan and directed how you want your property and other assets to be distributed, there is one other entity that must be considered which is your tax liability. If your taxable estate exceeds a certain value, your heirs may need to pay federal estate taxes or an inheritance tax at the federal and state level.

When you think about that, there's really only three ways to pay for those estate taxes. You can either pay in cash, which may not be possible for many families because once that money is gone, it's gone forever. You can either sell some assets, like your home or other assets, to gain the liquidity for tax purposes and this isn't going to be ideal for families with businesses. Or third, you can purchase life insurance to pay any taxes due. In most cases this is the least expensive of the three options because if you have done your estate planning properly, your beneficiaries will receive that policy’s death benefit tax-free. In some cases, depending on the value of your estate, it may make sense to create an irrevocable life insurance trust, because this creates an exemption and removes that policy as being counted towards your estate. You'll likely want to talk to your financial advisor who shared this video with you.

Life insurance, though, really protects against that lifestyle damage. This is the biggest adversary and concern for people doing estate planning. When you add up the assets, you'll see that the value of those assets won't sustain the lifestyle for your survivors in the manner that they're used to. Of course, you also need to consider final expenses, end of healthcare, and funeral costs. If you're still working when you do your estate plan, you'll see that the biggest asset is your future earnings.

Let's take an example. If you earn $100,000 per year and you have 25 years left before you retire, those future earnings are worth $2.5 million, not taking into account any future increases. Having enough life insurance in place for the payout to replace that income will safeguard your family's lifestyle. They'll be able to continue to stay in the same home if they want, pay for their children's education, pay for those medical expenses, and help them enjoy life without financial stress.

Now becomes the question, which type of life insurance do I need? This really is the two biggest hurdles for people buying life insurance. I again encourage you to reach out to the advisor sharing this video with you to determine your unique situation. There are two main types of life insurance. There's term insurance, which a lot of people are familiar with. This is an agreement with the life insurance company to cover the policyholder for a set number of years. This is the most common is a 10-year term and this insurance provides a death benefit only without any cash value. It tends to be the most affordable, more so than permanent, and can be a little bit more budget friendly. Those premiums remain level throughout that duration but can increase in the later years.

The second is permanent life insurance, specifically indexed universal life, which is known as cash value life insurance, and this is a form of coverage that covers the policyholder their entire life. It combines the death benefit with cash value accumulation and with an index universal life, your policy follows the growth of a specific index by which your cash value can grow overtime. Premiums remain flexible, but this type of insurance is more expensive than term insurance, but offers growth, tax, free distributions and most importantly, a tax-free death benefit upon your passing. Lastly, let's review some of the basic considerations when preparing your estate plan. If you get nothing else from this episode, I encourage you to do at least these three things.

First is draft a will. A will is a fundamental document that outlines how you want your assets to be distributed after your death. You want to clearly state who should inherit specific assets and designate an executor to carry out your wishes. If you have minor children, appoint a guardian to take care of them in the event of your demise. This is something you're going to want to regularly review and update to reflect any changes in your circumstances.

Two is choose beneficiary designations. Ensure that your beneficiary designations on accounts such as life insurance policies, retirement accounts, and bank accounts are all up to date. Clearly specify primary and contingent beneficiaries for each of those accounts and keep those designations consistent among your overall estate planning goals.

Lastly, assign your healthcare directives. Creating a healthcare directive such as a living will or a healthcare power of attorney to communicate your medical treatment preferences. You can designate someone who you really trust to make medical decisions on your behalf. If you're ever unable to do so. Share some of these documents with your healthcare providers and family members, ensuring what they're aware of and what your wishes are.

In conclusion, your financial legacy really starts here. When you think about it, your financial legacy is a personal narrative, and crafting a plan that aligns with your aspirations is your financial team's commitment to you, whether that's through personal consultation or online research that you may do. Your team is here to guide you towards a secure and an empowered financial future, so let's start shaping your legacy together. Thank you for tuning in and we'll see you next time.