Episode #319 – Why Your Estate Plan Needs to be Flexible

Hello and welcome to another edition of Money Script Monday. My name is Sean Brady, and today's topic is “Why Your Estate Plan Needs to be Flexible.” One key factor to keep in mind as you consider plans for transferring wealth to the next generation or passing on the family business is this - change is inevitable. As Greek philosopher Heraclitus said, “the only constant in life is change.” Your family dynamics may change. Your financial needs may change, and tax laws may and probably will change. There is one aspect of the estate planning that is unique and simply unknown. The timing of when your plan will go into effect, meaning your death.

These factors can create a moving target when it comes to developing an estate plan, making it important to build in as much flexibility as possible. Families often seek to accomplish one or more of the following with their estate plans: minimizing taxes, income tax, capital gains tax, state tax, gift tax and generation skipping taxes. You also want to protect your property from potential creditors, judgment creditors, bankruptcy trustees, a divorced spouse maybe. You want to assure that their estate ends up in the right hands. You want to avoid family strife, avoid mismanagements of their states by their heirs, and you want to keep the family business in the family.

While there are several strategies for accomplishing such goals, many require that irrevocable decisions to be made with very little ability to make modifications should circumstances change. But there are ways to implement strategies that could provide a level of flexibility allowing families to accomplish their goals while retaining the following: you're going to want continued use and enjoyment of property, continued access to income, the ability to control and manage property, and the ability to change future recipients of income and property.

The three reasons for building flexibility into your estate plan are changes in tax laws, changes in family dynamics, and changes in needs. Now, first changes in tax laws. The current federal estate tax originated from tax laws passed in 1916 and has gone through constant streams of changes over the past few days. Aids. There's been attempts to repeal the tax, changes to the exemption amounts, and changes to the tax rates. Since 2001, there have been three major pieces of legislation that have impacted federal transfer taxes. First, the Economic Growth and Tax Relief Reconciliation Act of 2001. The Tax Relief, Unemployment Insurance Reauthorization and Jobs Creation Act of 2010, and lastly, the 2017 Tax Cuts and Jobs Act. Many of the provisions in the 2017 tax acts relating to the estate and gift tax are set to expire in 2026.

There have been multiple attempts to change other laws related to taxes impacted by death. When a capital asset is passed at death, the basis of that asset is increased or decreased to the fair market value of the asset at the date of the death, often referred to as the step up in basis rule. Now this provides a tremendous advantage for the heir, who may then sell the asset and recognize little or no capital gains tax. It essentially wipes out all taxable gains on that asset. This step up in basis rule has been repealed once before, then reinstated and now proposals to repeal it again. That's a whole lot going on with tax laws.

Let's talk about the second change, changes in family dynamics. Families may go through many different changes as time goes on. Some are positive; grandchildren come into the world, marriages add new family members, and family business success is achieved. There's also some negatives; divorce separates families, family friction creates rifts, and family members may pass away well before their time. Now, with each change, your goals for passing on the wealth you've accumulated may change as well.

Consider the business owner with three children. Which child, if any, will want to take over that family business? What if the business owner decides to sell the business to a third party and the estate no longer includes a business interest? What if a grandchild is born with special needs? Now, would a traditional estate plan include provisions that address the unique financial needs of that child? These examples stress the importance of building flexibility into your plans.

Finally, changes in needs. Many of the more common estate planning strategies involve the transfer wealth prior to death. These may include strategies to gift assets, or sell assets, or loan funds to family members. Before making such a big decision, such a transfer, families should really analyze their own financial income needs and consider how those needs could potentially change. Gifting strategies may reduce your estate taxes and protect family wealth from creditors, but what if your financial needs change? What if there's a business failure, an economic downturn, or unexpected disability, and you need access to those gifts that you made?

It's really important to note that there are strategies that may allow you to achieve the advantages of a lifetime transfer of wealth while retaining a level of access to the funds transferred if needed. In each of the cases, an indexed universal life insurance policy could be an excellent funding vehicle because it offers tax-free death benefit, tax-deferred growth of cash value, and tax-free access to funds if needed. Now that concludes today's presentation. I really hope you found it of value and we'll see you again next time on Monday Script Monday.