CHAPTER 14: ESTATE PLANNING

MATCHING

a. marital deduction
b. charitable remainder
c. gift splitting
d. present interest
e. legal life estate
f. stepped-up basis
g. general power of appointment
h. term life insurance
i. disclaimer
j. bypass trust

1. An increase in the income tax of appreciated property, which is valued on the date of the donor’s death or the alternate valuation date

2. The right of a beneficiary or heir to refuse a gift by will, trust, or inheritance without any adverse tax consequences

3. An unlimited amount of a decedent’s gross estate that may be given to the surviving spouse without being subject to federal estate tax

4. An immediate and unrestricted interest in real or personal property

5. An estate created by operation of law and not directly by the parties themselves

6. The least expensive form of life insurance, which provides pure protection without cash surrender or loan value

7. A trust in which the settlor or named beneficiary can retain income from the trust, usually for life, and after death, the trust property goes to a qualified charity

8. An estate planning device whereby a portion of a deceased spouse’s estate passes to a trust instead of directly to the surviving spouse

9. The right to pass on an interest in property to whomever a donee chooses, including himself/herself, the estate, creditors, or creditors of the estate

10. A practice available to spouses to join in annual gifts and combine their individual gifts to donees to avoid gift taxes

1. ANS: F
2. ANS: I
3. ANS: A
4. ANS: D
5. ANS: E
6. ANS: H
7. ANS: B
8. ANS: J
9. ANS: G
10. ANS: C

TRUE/FALSE

1. Only attorneys are qualified to give estate-planning advice.
   ANS: F
   False
   Correct. Accountants, investment advisers, financial planners, and others are qualified to do so.
   True
   Incorrect. Trust officers at banks often give such advice.
2. When it is designed appropriately, an estate plan should meet all the testator’s objectives and provide him/her with a comfortable retirement income.
   ANS: T
   True
   Correct. The estate plan should also provide financial protection for the testator’s family.
   False
   Incorrect. The estate plan should also involve a minimum of taxes and expenses throughout its implementation.

3. After it is established, an estate plan does not need to be reviewed again until the testator’s death.
   ANS: F
   False
   Correct. Changes in family relationships may require a review of the estate plan.
   True
   Incorrect. Changes in tax laws also may require a review of the estate plan.

4. A charitable remainder annuity trust allows for additional contributions to be made to the trust property.
   ANS: F
   False
   Correct. Such a trust does not allow for additional contributions.
   True
   Incorrect. A charitable remainder unitrust allows for additional contributions.

5. Gifts of future interests do not qualify for the annual gift tax exclusion.
   ANS: T
   True
   Correct. Gifts of future interests are not immediate.
   False
   Incorrect. The annual gift tax exclusion is available only for present interests.

6. Estate planning must always take place before the death of a testator.
   ANS: F
   False
   Correct. Postmortem estate planning is often used for tax-saving purposes.
   True
   Incorrect. Postmortem estate planning might, for example, include the disclaiming of an inheritance.

7. If a same-sex couple has a legally recognized civil union in their home state, they qualify for the federal marital deduction.
   ANS: F
   False
   Correct. Partners of civil unions and domestic partnerships do not qualify for the marital deduction.
   True
   Incorrect. This deduction is limited to married couples.

8. If a husband gives his wife a gift of $500,000, neither party has to pay federal gift tax.
   ANS: T
   True
   Correct. Nor must either party pay estate tax.
   False
   Incorrect. Outright transfers between spouses by gift are not subject to federal gift and estate taxes.

9. An elderly beneficiary may choose to disclaim an inheritance.
   ANS: T
   True
   Correct. Age, health, and financial security are common reasons for disclaiming an inheritance.
   False
   Incorrect. Anyone can legally disclaim an inheritance.
10. Estate administration expenses can be used as a deduction for estate tax purposes.  
   **ANS:** T  
   **True**  
   Correct. These expenses may alternately be used as a deduction for income tax purposes.  
   **False**  
   Incorrect. These expenses can be used as a final postmortem tax-saving method.

**MULTIPLE CHOICE**

1. Which is NOT a potentially adverse factor that could diminish any estate?  
   a. Administration expenses  
   b. Trusts that transfer property after the deaths of both spouses  
   c. Forced liquidation  
   d. Termination of employment  
   **ANS:** B  
   **Trusts that transfer property after the deaths of both spouses**  
   Correct. Such trusts are not subject to estate taxes.  
   **Administration expenses**  
   Incorrect. These expenses must be paid from the assets of the decedent’s estate and may substantially lessen its value.  
   **Forced liquidation**  
   Incorrect. The personal representative may be forced to sell assets to pay legitimate expenses.  
   **Termination of employment**  
   Incorrect. Such termination creates a substantial loss of income to the estate.

2. As part of an estate plan, a will allows the testator to:  
   a. Protect a spendthrift child  
   b. Preserve privacy  
   c. Appoint both personal and property guardians for minor children  
   d. Provide a lifetime income for the surviving spouse  
   **ANS:** C  
   **Appoint both personal and property guardians for minor children**  
   Correct. A single person may be appointed for both positions, if the testator so desires.  
   **Protect a spendthrift child**  
   Incorrect. A spendthrift trust protects a spendthrift child.  
   **Preserve privacy**  
   Incorrect. A will is a public document.  
   **Provide a lifetime income for the surviving spouse**  
   Incorrect. A will allows the testator to leave an entire estate to a surviving spouse, but the property of the estate must be invested separately.

3. Which is NOT a way in which an estate planner can use trusts to benefit family members?  
   a. Identify the estate assets and the beneficiaries who are to receive them.  
   b. Diminish problems such as will contests.  
   c. Reduce federal and state death taxes.  
   d. Avoid probate.  
   **ANS:** A  
   **Identify the estate assets and the beneficiaries who are to receive them.**  
   Correct. This is a provision of a will, not a trust.  
   **Diminish problems such as will contests.**  
   Incorrect. Trusts cannot be contested in court.  
   **Reduce federal and state death taxes.**  
   Incorrect. Trusts can be used to increase the marital and charitable deductions.  
   **Avoid probate.**  
   Incorrect. Wills—not trusts—must be probated.

4. Which is NOT a common method of reducing the gross estate?  
   a. Life insurance  
   b. Trusts that do not avoid multiple taxation  
   c. Gifts made during the donor’s lifetime  
   d. Special power of appointment  
   **ANS:** B
Trusts that do not avoid multiple taxation
Correct. Trusts that avoid multiple taxation or qualify for the marital deduction reduce the estate.

Life insurance
Incorrect. Life insurance payments can be used to pay debts and expenses.

Gifts made during the donor’s lifetime
Incorrect. A gift made before the donor’s death reduces the estate by the value of the gift.

Special power of appointment
Incorrect. This excludes the value of the property appointed for being included in the gross estate of the spouse, who is the beneficiary.

5. Which is NOT a major type of life insurance?
   a. Universal life insurance
   b. Whole life insurance
   c. Term life insurance
   d. Custodial life insurance
   ANS: D
   Custodial life insurance
   Correct. Custodial life insurance is not a classification of life insurance.
   Universal life insurance
   Incorrect. Universal life insurance covers a specific period and builds the cash value of the policyholder.

Whole life insurance
Incorrect. Whole life insurance combines lifetime protection with a minimum savings feature called cash value.

Term life insurance
Incorrect. Term life insurance is pure protection without savings.

6. To qualify for the charitable deduction, a gift cannot be made to a(n):
   a. Private school
   b. Religious charity
   c. Individual
   d. Librar
   y ANS: C
   Individual
   Correct. A charity cannot be an individual.
   Private school
   Incorrect. The charitable deduction applies to gifts made for educational purposes.
   Religious charity
   Incorrect. The charitable deduction does not discriminate on the basis of religious beliefs of an organization.
   Library
   Incorrect. Gifts made to provide a literary benefit qualify for this deduction.

7. Which of the following is NOT a benefit of a charitable remainder trust?
   a. It acts as a form of life insurance that benefits the settlor’s children.
   b. It reduces income tax.
   c. It increases current income by providing life income for the settlor.
   d. It reduces federal estate tax liability. ANS: A
   It acts as a form of life insurance that benefits the settlor’s children.
   Correct. When the settlor dies, the money goes to a charity.
   It reduces income tax.
   Incorrect. It allows the settlor-donor an income tax deduction for the gift.
   It increases current income by providing life income for the settlor.
   Incorrect. It provides a life income for the settlor by using property that currently does not provide income.
   It reduces federal estate tax liability.
   Incorrect. Gifts to charities, in general, are exempt from federal estate tax.

8. Which of the following is a feature of a Charitable Remainder Annuity Trust?
   a. It is revocable.
b. Payments to the beneficiary vary annually.
c. It counteracts the effects of inflation.
d. Additional contributions cannot be made to the trust property. ANS: D

Additional contributions cannot be made to the trust property.
Correct. Additional contributions can be made to a Charitable Remainder Unitrust but not to a Charitable Remainder Annuity Trust.

It is revocable.
Incorrect. A Charitable Remainder Annuity Trust is irrevocable.
Charitable Remainder Annuity Trust.

Payments to the beneficiary vary annually.
Incorrect. This is a feature of a Charitable Remainder Unitrust.
It counteracts the effects of inflation.
Incorrect. This is a feature of a Charitable Remainder Unitrust.

9. The practice of gift splitting is available only between:
   a. Spouses
   b. A parent and a natural child
   c. A parent and an adopted child
   d. Siblings

ANS: A
Spouses
Correct. Spouses can give up to $26,000 together to a donee.
A parent and a natural child
Incorrect. Gift splitting can be done only between spouses.
A parent and an adopted child
Incorrect. Gift splitting can be done only between spouses.
Siblings
Incorrect. Gift splitting can be done only between spouses.

10. A QTIP trust must:
   a. Be in the form of a testamentary trust
   b. Give the surviving spouse the right to all the income from the trust property for life
   c. Allow the trustee to use any amount of the trust principal for any purpose
   d. Give the surviving spouse a general power of appointment

ANS: B
Give the surviving spouse the right to all the income from the trust property for life
Correct. This income must be payable at least annually.
Be in the form of a testamentary trust
Incorrect. The QTIP trust can be a testamentary or living trust.
Allow the trustee to use any amount of the trust principal for any purpose
Incorrect. Some of the trust principal must be used only for the surviving spouse’s health, education, support, or maintenance.
Give the surviving spouse a general power of appointment
Incorrect. The settlor-spouse determines the trust property distribution after the death of the surviving spouse through the trust.