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A Death in the Family – Now What?

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A death in the family is an emotional time, and often the task of closing out the decedent's life is an overwhelming and stressful responsibility left to the decedent's loved ones. Advance planning for the administration of your assets at your death can provide stress relief and a clear path forward. Estate planning may also alleviate the tax burden to your loved ones and allow your legacy to remain intact for future generations.

Below are some considerations when there is a death of a family member or loved one:

To Do Immediately:

- Search for the decedent's Advance Health Care Directive for instructions regarding burial and organ donations – the named agent has the authority to make these decisions
- Notify friends and family
- Secure and lock up property
- Consider funeral and burial preparations
- Prepare an obituary
- Search for the decedent's will and other estate planning documents
- Notify Social Security, Medicare, etc.
- Stop health insurance
- Look into death benefits through employer
- Notify life insurance companies
- Make a list of important bills (such as mortgage payments and property insurance) to ensure that bills are appropriately handled
- Notify mortgage companies, banks and credit card companies
- Notify credit reporting agencies
- Meet with an estate planner to discuss the administration of the estate. There are plenty of tax and state law rules that require attention and compliance.

Trust or Probate Administration?

If the decedent created a revocable trust during life with a "pour-over" will, then the decedent's estate will be administered according to the trust, most likely with no court intervention. If a decedent did not establish a revocable trust or left a probate estate, then a probate administration should be commenced with the applicable Superior Court.

In a trust administration, a successor Trustee can immediately begin acting on behalf of the Trust. The successor Trustee can take control of Trust bank accounts and other assets, act on behalf of the Trust with respect to closely held business interests and otherwise manage the Trust's affairs almost seamlessly. Assuming there are sufficient assets in the Trust, distributions to the decedent's beneficiaries can be accomplished in short order. All of this can be done without court supervision and without making a public record of the decedent's assets and liabilities.

On the other hand, in a probate administration, an interested person must petition the probate court to commence an estate administration and appoint a personal representative, which can take months. An inventory of the decedent's assets and liabilities will be filed with the court and open to public inspection, and all actions are subject to judicial scrutiny. It can easily take more than a year to distribute the assets and close the probate administration – probate courts in Los Angeles and Orange Counties are quite backlogged.

Will the IRS Take All the Family Money?

Income Taxes. Some may expect to get a hefty income tax bill when they receive an inheritance. However, the recipient of an inheritance does not generally pay California or Federal income taxes on the bequest. (Retirement plan assets are the big exception to this rule.) Furthermore, the income tax basis of the assets received through inheritance are "stepped up" to fair market value at date of death, potentially eliminating significant capital gain on the subsequent sale of such assets.

Keep in mind, however, if you inherit something that has produced income since the date of the decedent's death, that income could be taxable to you.

So-called "Death Taxes" (aka Estate Taxes). There is no California estate tax or inheritance tax, so families of California decedents generally need only focus on Federal estate taxes.

The American Taxpayer Relief Act of 2012 (ATRA) set the Federal gift and estate tax exemption and the generation-skipping transfer tax (GST tax) exemption at $5 million, indexed for inflation. For 2016, the gift and estate tax and GST tax exempt amounts all equal $5.45 million (which means $10.9 million for married couples). For individuals with a net worth under $5.45 million (reduced by lifetime taxable gifts), there will be no estate tax or GST tax at the taxpayer's death.

For larger estates, the estate and gift taxes and GST taxes are all set at a flat 40 percent rate. This means an individual with a net worth of $15 million and a fully taxable estate could expect a Federal estate tax bill of up to $3.82 million upon death. For those with a net worth above the exemption amount (or those expecting an event to cause their net worth to exceed the exemption amount), a check-up with your estate planner is advised to ensure that your plan takes appropriate advantage of today's laws and the cutting edge techniques that can reduce the future transfer tax bill from the IRS.

To File or Not to File an Estate Tax Return

If a decedent leaves an estate over the exemption amount (reduced by taxable gifts), a Federal estate tax return must be filed. Some estates under the lifetime exemption amount should also file a Federal estate tax return to elect "portability."

ATRA made "portability" permanent – a great benefit to married couples. If a spouse dies without exhausting his or her lifetime gift and estate tax exemption, so long as the decedent's executor makes the proper election on an estate tax return, the unused exemption is credited or "ported" to the surviving spouse for use during life or at death. The deceased spouse's unused exemption at the survivor's death will be combined with the survivor's own estate tax exemption to offset any estate tax liability in the survivor's estate.

Keep in mind, however, unused GST exemption is not portable; if it is not used by the decedent, it is lost. Families wishing to engage in multiple generational planning should consult with their estate planner.

Finally, a new Federal law passed in 2015 provides that executors of an estate and others may be required to file IRS Form 8971, which reports information on property acquired from a decedent by a beneficiary. Form 8971 is intended to ensure consistent income tax basis reporting by estates and their beneficiaries. The Treasury Department and the IRS expect to issue proposed regulations to provide more guidance on such reporting shortly.

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