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THE ABSOLUTE ESSENTIALS OF ESTATE PLANNING FOR SAME-SEX AND UNMARRIED COUPLES

You know the law treats you differently from married couples. Here's what you can do about it.

by Ron L. Meyers

Marriage is the single most significant factor in estate planning. While your personal wealth may determine how much you will pay in taxes, your marital status determines whether or not the tax applies to you in the first place. A spouse occupies the absolute first position for inheritance and many other functions, ahead of all other relatives; an intimate partner who is not recognized as a spouse occupies no position at all for inheritance, with all the relatives taking higher priority. If you are not married in a way that is recognized by the state *and* federal governments, you are operating on a different terrain from your married friends, and it's important to plan accordingly. For this reason, it's important for same-sex couples to have **professional advisors who are not only gay-friendly, but gay-knowledgeable**. Here are the essential factors you must consider in your planning:

1. WHO RECOGNIZES YOU? An increasing number of states are extending legal recognition to same-sex partners, but while the situation is dynamic, it is also unstable, and the recognition is often incomplete. Some states offer domestic partnerships or civil unions, rather than marriage. These types of status may offer the same protections as marriage – or they may not. Because they are called something other than marriage, they can be defined in the law differently from marriage, and the definitions may change over time as a result of legislation and court decisions. Moreover, a state that has civil unions may or may not recognize a domestic partnership, and vice-versa. New York does not currently allow same-sex marriages to be solemnized in the state, though it does recognize same-sex marriages performed out of state. But because the terms "domestic partnership" and "civil union" do not exist in the laws of New York, these types of status receive no recognition. The federal government – which controls Social Security, immigration, and many tax matters, to name just a few functions – does not recognize same-sex marriages at all. And this can influence the results of state law, even where same-sex marriage is recognized. For example, New York will recognize your same-sex marriage, but will still require you to file taxes in the same manner as you file your federal taxes, thus foreclosing any marital benefits that the state's marriage recognition might have offered. Recent changes in the law are very positive and exciting – but they are complex. Don't let them give you a false sense of security.

2. WHOM DO YOU WANT TO INHERIT YOUR ESTATE? Remember that your partner is nothing more than a stranger, friend or roommate to you in the eyes of the law. The friends or non-immediate relatives to whom you may wish to leave your assets have similar status for inheritance purposes. In order to ensure that your partner and other intended beneficiaries inherit your property, **it is vital that you have at least a will**. It is vital that the will be valid according to the legally required formalities, and that it be well crafted to account for an array of legal concerns, beginning with taxes. It's better to have a will than not to have one, but it's best to have one prepared by a qualified lawyer with specific knowledge and experience in this complex area, rather than to print one from the internet that may or may not address your needs.

Marriage is perhaps the best way for you and your partner to secure your rights to each other's estates, but only if the marriage will be recognized in the state where you live. As discussed above, marriage might not afford you all the advantages of other-sex marriage but it may give many of the essential benefits of priority in inheritance.

Another way to ensure that property passes to your partner without interference is to **own the property as joint tenants with the right of survivorship**. This means that each of you is simultaneously a 100% owner of the property – whether it be a house, a car, an investment account – and that upon one partner's death, the survivor continues to own it, with no possibility of any claims by other relatives, as might arise if the property passed by means of a will. But be careful: joint tenancy can introduce serious problems, especially with regard to taxation and separation, so enter a joint tenancy only with careful professional attention to its implications.

If you have retirement plans through your employer, such as a 401(k), the ways the account can be inherited by a non-spouse beneficiary may be severely limited, and may involve serious loss of the inheritance to taxes, so check with your plan manager about the specific rules. If possible, **roll your retirement funds over into an IRA**. With an IRA, you can consolidate all your retirement assets, utilize a much wider range of investment options, and enjoy much more favorable inheritance rules, which will not leave your partner out in the cold. With all retirement accounts and life insurance policies, **make sure that your beneficiaries are properly designated** – check with the plan manager to ensure that the language you have written in your designations will have the intended effect. Review your beneficiary designations annually to ensure that they remain in effect (since plan rules and managers change over time) and that they continue to reflect your current wishes (since partners may change over time, too).

There are many people other than your partner to whom you may wish to distribute your estate. But there are a number of issues to keep in mind when doing so. If anyone among your beneficiaries may be a minor – this may include, for example, your sister's kids if your sister is a beneficiary and she predeceases you – then it's important to name a trustee to hold the funds until they are adults. If you intend to leave assets to children with whom you have a parental, but not a biological, relationship– such as stepchildren, or your partner's biological or adopted children– then the background law will afford them no standing to inherit your estate. It is vital that you name them in a valid will, and perhaps also in a **revocable living trust**, to help ensure that other relatives cannot scuttle the gift. Best of all is to establish a legal relationship with the child through **adoption**, which may include second-parent adoption. If any of your beneficiaries is disabled and receiving public benefits, your gift may give them enough assets to lose their eligibility for those benefits, unless the gift is made to a **special-needs trust**. And if beneficiaries of substantial assets, other than your own children, might be more than 37 years younger than you (again, think of your sister's kids), there is a harsh **generation-skipping tax** that you will want to avoid through additional planning.

3. WHOM DO YOU <u>NOT</u> WANT TO INHERIT YOUR ESTATE? If you have any close relatives who might seek to interfere in your inheritance plans – if there's anyone among them who objects to your "lifestyle", who doesn't like your partner, who holds a family grudge, who is less well-off than you and may see an opportunity to profit from your estate – then you may want to have a **revocable living trust** in addition to a will. Assets passing according to a will are distributed through a court-supervised **probate process**, in which certain relatives have standing to stake a claim to your estate. The trust creates an alternate structure of ownership for your assets, which allows for a non-probate distribution process that involves no one but your named beneficiaries. It's not an absolute shield from family interference – nothing is – but it sets the bar much, much higher.

If you don't want the IRS to inherit your estate, it's important to create structures that will enable to you **minimize estate, gift and inheritance taxes**. Various taxes are imposed at the state and federal levels, and they can function cumulatively, with, for example, a 15% state tax and a 45% federal tax being levied on the same assets, leaving little or nothing to your beneficiaries. There are numerous, perfectly legal tax-reduction strategies that can be enacted with little or no change in the way you use your assets now, or in the way your beneficiaries can enjoy them later.

If you break up, you probably don't want your **former partner** to inherit your estate. One of the surprising benefits of marriage is the orderly legal process of divorce in the event of a separation. If you marry, then you will enjoy this process of dividing property, neatly and conclusively, upon a separation. If you do not marry, then you are on your own to negotiate the separation of property with your estranged partner. But whether married or not, all transfers of property in the dissolution of a non-federally-recognized relationship are potentially taxable gifts. It is wisest to plan in advance for the possibility of a separation by executing a prenuptial or domestic-partner agreement, and by structuring property ownership in a way that will allow an orderly division. **Joint-tenancy** ownership, mentioned above as a good way to ensure seamless succession, is extremely difficult to unwind, so the arguments against it may be as strong as or stronger than the arguments for it.

4. WHAT MARRIED FOLKS HAVE THAT YOU DON'T HAVE. Within a federally-recognized marriage, spouses can transfer property to each other – houses, jewelry, cars, investments – absolutely free of taxes. Transfers of property between anyone else is a gift. Gifts over a certain amount in any calendar year (for 2009 it's $13,000) are reportable to the IRS, and will increase your exposure to federal estate taxes. Reported gifts that accumulate to more than $1M over your lifetime are taxed at 45%. And gifts include *all* transfers of value, not just exchanges of property – if one partner pays for both to go on vacation, that is a gift; if one partner is named on the mortgage and the other partner pays it, that's a gift, too. It may not be necessary to keep your assets as rigorously separate as to split the bill for dinner, but a tax audit could bring questions as minute as these into play. Your lawyer and accountant can help you enact the appropriate levels of caution in your day-to-day dealings.

There is no estate tax on any property passing from a deceased spouse to the surviving spouse. Property passing to anyone other than a spouse is subject to estate tax. And same-sex marriage at the state level gets you only so far – since federal law does not recognize same-sex marriage, you do not have marital benefits in your federal taxes. And, as noted above, the New York tax laws apply principles of federal law, so even state-level benefits are not available unless and until the laws are changed.

As noted above, the benefits of marriage include the benefits of divorce, which include decisive and tax-free distribution of marital property. If you have state-level recognition for your relationship, you may enjoy the protections of your state's divorce laws. But again, the federal exemption from income and gift taxation upon the distribution of property in divorce is not available to you, so you must still do things differently, with the guidance of gay-knowledgeable advisors.

5. LIFE BEFORE DEATH. Estate planning does not focus only on what happens after your death. Aspects of estate planning are essential for the management of your most intimate affairs while you are alive, and it's important to attend to these concerns, even before writing your will. It is only through **health care proxies** and **living wills** that you can designate someone to make decisions for you about medical treatment and end-of-life care. Even marriage does not confer the authority to make these decisions as seamlessly and as decisively as these documents. For all your other affairs, a power of attorney enables you to authorize someone else to handle personal business for you if you are unable to

manage it yourself. If you are in the hospital and need to submit insurance forms that are essential to the care you are receiving, your power of attorney would enable your agent to open your mail, sign the papers, make the payment, and get it done. These "living documents" are vital for everyone, rich or poor, old or young, married, partnered or single. No one should be without them.

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These are the headlines about organizing your affairs in light of the current laws, which sort-of do and sort-of don't recognize non-traditional relationships. My frequent references to the advice of professional advisors are not intended as a plug for business, but rather as a reminder that these things are complicated and, like medical care, call for knowledgeable and insightful guidance. Even professional advisors – lawyers, accountants, financial planners – must put their heads together to analyze a situation fully and implement appropriate protections, so the best approach is to engage a team of people whom you trust to work out a plan for you, and then to review it together comprehensively from time to time. Any professional who practices in this area can tell tragic stories about people who have been left out of their partner's estate, who were unable to recover their property after a break-up, or who were unable to help their partner during an illness. There are many kinds of problems that can be prevented in advance, but simply, absolutely cannot be solved after the fact. You don't want your story to play out this way, especially if a few well-crafted documents can make the difference.

Ron L. Meyers is an estate-planning attorney who uses legal planning, tax reduction structures, and charitable and strategic gifts to help clients make the most of their assets for themselves and their loved ones, during their lives and beyond. This article is presented for educational purposes only; it is not intended as, and should not be construed as, tax advice.

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