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**Surviving after death – how to avoid
nightmare estate**

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Preparing love and death: Prenups and estate agreements

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Preparing love and death: Prenups and estate agreements

- Case study and questions
- Approach in each jurisdiction
- Impact of solutions in other jurisdictions
- Q&A

Case Study

- Husband (48) and Wife (42)
- Married for 18 years
- Two children, Jane (16) and Janet (13)
- Wife has a son from a previous relationship, Nicholai (24)
- No pre-nup or marital contract
- Wife is a part time teacher with little wealth of her own
- Husband is a successful self-made businessman – you can download his app from the App Store

Case Study (cont'd)

- Husband's assets:
 - Business = GBP10m/USD13.3m/EUR11.3m
 - Family home = GBP1m/USD1.3m/EUR1.1m
 - Summer house = GBP600k/USD800k/EUR680k
 - Cars and chattels = GBP200k/USD268k/EUR226k
 - No life insurance or pensions
- Husband takes a reasonable salary and dividends where necessary
- One of the couple may come to receive a large inheritance from her/his parents



Case Study Questions



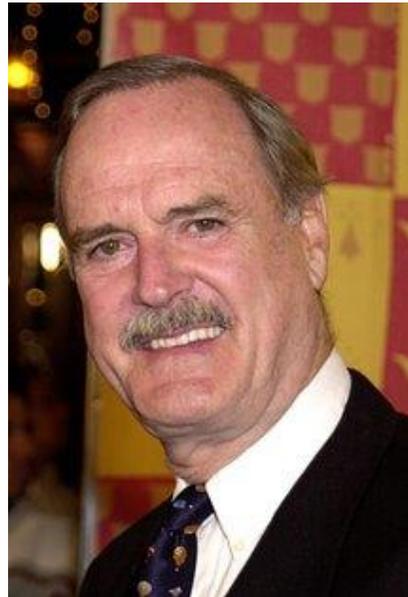
1. What would Wife be entitled to if Husband dies intestate tomorrow?
2. How would you advise Husband in order to secure his assets (including his business assets) in case of divorce but provide reasonable financial provision for Wife and the children in case of his death? Which documents/agreements/vehicles would normally be considered relevant?
3. How would the solutions presented by the other panel speakers work in your jurisdiction if Wife moves to or acquires assets in your jurisdiction?



UK: Good morning, Valbella



Meet John and Mary Smith...



UK: Mary's entitlement on intestacy



- Statutory provision for spouse with children:
 - Chattels outright
 - £250,000 legacy outright (plus simple interest)
 - One half of residue outright
 - Remaining one half of residue to issue on statutory trusts
- Inefficient for inheritance tax ('IHT') purposes
- Query whether John would have wanted Mary to receive assets outright



Post-nuptial agreement

- Not automatically legally binding
- May be upheld if:
 - Independent legal advice
 - Full and frank financial disclosure (including potential inheritance)
 - Freely entered into
 - Neither party left in real need, i.e. no unfair terms
 - Children properly provided for up to the age of 18 years



Will

- Very important!
- Suggest taking advantage of spouse exemption for IHT purposes
- Life interest for Mary may be preferable for asset protection reasons
- Note 1975 Act claim if lack of reasonable provision for spouse and/or dependants



Trust for shares

- Trust for some or all of the shares
- If attract business property relief for IHT purposes
- May be created during lifetime or under Will
- John and Mary could be excluded – more tax efficient and greater protection on divorce



Share reorganisation

- Split shares into different classes:
 - 'A' shares – voting/control rights
 - 'B' shares – economic rights
- Transfer (some) B shares to Mary and/or children



Life insurance

- E.g. to cover IHT on second death
- Write into trust to take outside of estate for IHT purposes

Pension

- E.g. to make provision for Mary on John's death
- Terms of pension should mean outside of estate for IHT purposes



Meet John and Maria Smith...



US: Maria's entitlement on intestacy



- Applicable law is state of domicile at death
- South Carolina – estate of person dying intestate with children passes one-half to surviving spouse, one half to children; if no children, entire amount to surviving spouse; if unmarried, closest family
- Shares for minor children difficult without planning; in this case, could be nearly \$8,000,000 in assets
- US estate tax exemption just increased to \$11.2 million per spouse (\$22.4 million per married couple)

US: Suggested solutions for John 1



Will, could be combined with revocable trust agreement (RTA)

- RTA would contain operative provisions, provide privacy for family, potentially save on state probate court fees if RTA is funded; grantor still treated as owner for income tax purposes
- Common structure – 1/2 to spouse (outright or in trust) and 1/2 to children (likely in trust); John may or may not want to benefit Maria's child, so structure could be devised to accommodate his wishes
- Many old estate planning structures contain bypass trusts formed before portability of estate and gift tax exemption



Trusts for children

- Can provide income distributions to or for the benefit of the children with principal available as parents see fit (education, health care, support/maintenance, assistance with primary residence, etc.)
- Often, trusts provide for portions of principal to be paid out at certain ages (i.e., 1/2 at 30, 1/2 at 35)



Potential planning for divorce

- Providing in will and trust documents that any benefits to spouse are contingent upon being married (not legally separated?) at the time of death
- Postnuptial agreement



Postnuptial agreement

- Less common than prenuptial agreements but generally enforceable if requirements satisfied
- Objectives: (1) narrow definition of marital property that family courts have jurisdiction to divide in case of divorce (inheritance should not be marital property, but commingling can convert), (2) waive any rights to elective share (South Carolina = one-third, Colorado = 5% per year of marriage up to 50%), (3) waive some or all rights to alimony awards in case of divorce
- Requirements – (1) full, open financial disclosures, (2) separate, independent legal counsel, (3) not unconscionable, (4) meaningful choice, no fraud or duress



Other Considerations

- Estate tax issues - \$22.4 million exemption
- Tradeoff – leaving assets to children (even in trust to benefit spouse for lifetime) removes appreciation from estate of subsequent spouse, BUT carryover basis applies for income tax purposes
- Lifetime gifting has same income tax basis issue

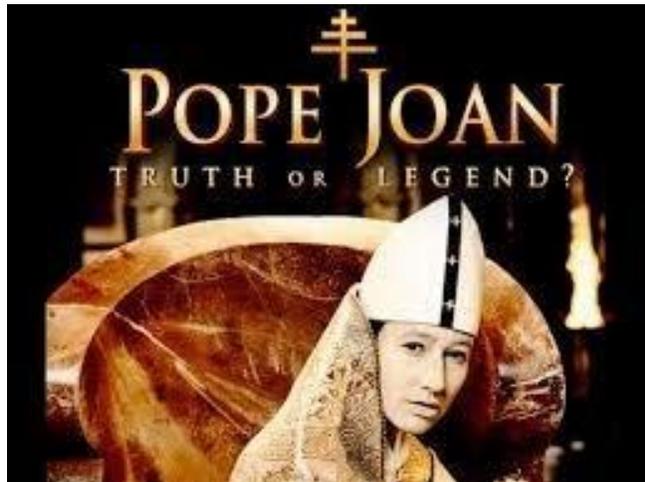


Other Considerations cont'd

- Exemption for estate and gift taxes is unified; gifts of \$15,000 per year per recipient (\$30,000 for married couple) do not reduce exemption
- Where clearly likely to have estate tax problem, transfer of appreciating assets to children can still make sense; discounting can apply to valuation
- Irrevocable life insurance trust could be prudent here
- GST trust could save estate taxes arising due to inheritance



Meet Joan and Mario Smith...



DE: Mario's entitlement on intestacy



- Mario: 50% of Joan's assets value = GBP 5.9 mio.
- Jane and Janet: 25% each
- Mario, Jane, and Janet form a community of heirs. Joint property of all assets. Each heir is entitled to claim to dissolve the community by selling assets.
- IHT:
 - Tax rate 19 %.
 - Tax free: Half of Mario's 50% share.
 - Tax free: EUR 500,000 for Mario and EUR 400,000 for Jane and Janet.

DE: Mario's entitlement in case of divorce



- Without marital agreement, Mario will be entitled to claim for financial compensation of 50% of increase in value of Joan's assets during marriage.
- Accordingly, Mario's payment claim shall amount to GBP 5.9 mio. This may jeopardize the existence of Joan's business.
- Even though Mario or Joan expect a large inheritance, this does not affect Mario's compensation claim in either way.

DE: Suggested solutions for Joan 1:



Somehow convince Mario to enter into a **marital agreement/post-nup**

- Post-nup legally binding under German law
- Joan's business (and its increase in value during marriage) shall be excluded from compensation in case of divorce.
- Contractual compensations to Mario may be considered (e.g. transfer of real estate, pension payments, maintenance etc.)
- Governing law / jurisdiction clause

DE: Suggested solutions for Joan 2:



Consider **transfer of business to trust** for the purpose of asset protection in case of divorce?

- It is a deep cut in Joan's assets: Joan may still control but will not own trust/business anymore
- In case of divorce, this transfer would only protect Joan against Mario's compensation claim either if Mario agrees to the transfer or if 10 years go by between transfer and divorce petition
- Hence: Transfer to trust behind Mario's back is not very effective to protect business in case of divorce



Will

- Trust vs Transfer to Mario/kid
- What does Joan prefer?
 - Business/assets protected and predetermined “forever”: trust
 - Mario/kids shall decide themselves: Transfer to Mario/kids

DE: Suggested Solutions for Joan 4:



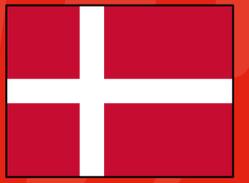
Will may provide for:

- Mario as sole heir, Jane/Janet only after Mario's death
- Exclude transfer to Nicholai via Mario
- Appoint a trustee to administrate the business shares for the heirs. How long?
Range of administrator's powers?
- Protect assets/business from extra-family influences (e.g. Jane/Janet's future spouses, creditors) by limiting Mario/Jane/Janet's rights to a fiduciary position for the next generation of heirs.

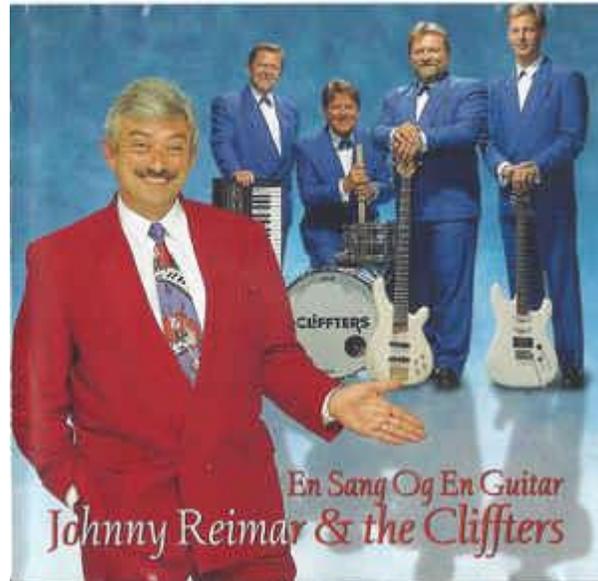


Tax

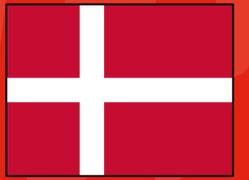
- Consider successive lifetime asset transfer to kids for tax reasons (EUR 400,000 per 10 years are tax free)
- Transfer to trust: No IHT advantage



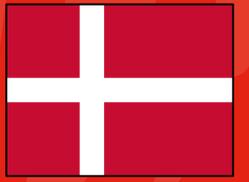
Meet Johnny and Mary Smith...



DK: Maria's entitlement on intestacy

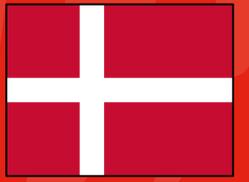


- Matrimonial property regime
 - Community property. Maria receives 50 % of John's net assets.
- Inheritance
 - Maria receives 50 % of the inheritance.
- Maria receives in all:
 - 50 % of John's net assets as her part of the community property and
 - 50 % of the remaining 50 % (= 25 % of the net assets)
 - Total: 75 % of John's net assets = GBP 8,850,000.
- Maria has the first right to choose assets – e.g. the business



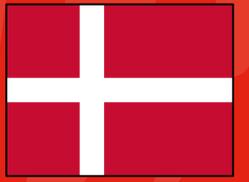
Post-nuptial agreement/marital contract

- Legally binding
- Community property changed to separate property or a combination
- Separate property on the inheritance from parents can be decided by the parents and not changed by Maria and John



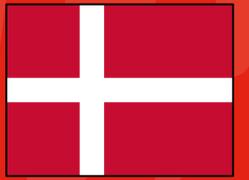
Will

- Very important!
- Maria's statutory rights
 - Personal items
 - If community property: 50 % + 1/8 of the rest = 9/16
 - If separate property: 1/8
- Right to choose for the children



Will

- Conditions for inheriting the business
 - Restrictions on certain decisions
 - Composition of the board
 - Restructuring
 - Shareholders' agreement
- Maria renouncing her statutory rights receiving fixed amount instead



Other dispositions

- Lifetime transfer or restructuring of the business
- Pension benefiting Maria
- Insurance benefiting Maria

UK: Impact of solutions in other jurisdictions



- Postnuptial agreements – court may be less inclined to uphold if agreement does not meet UK’s criteria
- Non-UK Will should be upheld if formally valid
- Succession laws of other jurisdictions may affect dispositions under UK Will – election under EU Succession Regulation?
- Consider impact on UK tax position, e.g. IHT trust charges, loss of spouse exemption, affect on BPR

US: Impact of solutions in other jurisdictions 1



- US documents can include governing law provision; so-called forum selection clause may come from another jurisdiction and would generally be respected
- Common exceptions: (1) if a party to a marital agreement did not receive fair and reasonable disclosure, (2) if agreement unconscionable, (3) if agreement deemed contrary to public policy
- Family courts more likely to consider equity and fairness (which creates unpredictability)

US: Impact of solutions in other jurisdictions 2



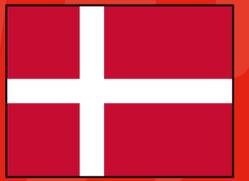
- US states normally respect a will validly executed under the laws of another jurisdiction, but foreign wills normally must be validated, and there can be exceptions (i.e., some states require at least two witnesses, no oral wills, etc.)
- Best practice is to coordinate wills with legal counsel from both countries (if relocation known/anticipated), with each referring to the will from the other country
- US estate and gift tax exemptions DO NOT apply to nonresident, noncitizens, so if John and Maria acquire US-situs assets such as US real estate or stock, they could trigger US estate tax (exemption only \$60,000); foreign hold company solution

DE: Impact of solutions in other jurisdictions



- Non-German marital agreements: Accepted by German courts if valid according to law of origin
- Marital property regime: German courts apply law of origin
- Non-German Will: Accepted if formally valid
- IHT: Subject to German IHT / double-tax agreements

DK: Impact of solutions in other jurisdictions



- Marital property regime is Danish if John lives in DK for 5 or more years
- Applicable law on succession according to Danish PIL = the law of John's domicile at the time of death. Could be Danish law => statutory rights according to Danish law
- Foreign wills normally recognised (according to 1961 Hague Convention)
- Foreign marital contracts/prenups/postnups may be recognised
- Trusts are normally not recognised in Danish law => severe tax consequences and statutory rights also with regards to assets held in foreign trusts
- EU regulations on marital property and succession do not apply in DK

Questions



Please feel free to ask us any questions, either now or over the course of the seminar.



Thank you!

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