

CFP Estate Planning Practice Test (Sample)

Study Guide



Everything you need from our exam experts!

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SAMPLE

Questions

SAMPLE

- 1. What happens if a parent dies before their child, according to the Predeceased Parent Rule for GSTT?**
 - A. The child must inherit nothing from the grandparent.**
 - B. The child can inherit directly from the grandparent.**
 - C. The child will only receive a limited inheritance.**
 - D. The child inherits only if there is a will present.**
- 2. In the net gift technique, what does the donee agree to do?**
 - A. Pay the estate tax**
 - B. Pay the gift tax**
 - C. Transfer assets to the donor**
 - D. Exclude the gift from taxable income**
- 3. What is true regarding the treatment of real estate in a gross estate?**
 - A. It is always excluded from the gross estate**
 - B. It includes worldwide real estate in the decedent's estate**
 - C. Only property located in the state is included**
 - D. Only commercial real estate qualifies for inclusion**
- 4. What is the implication of the joint tenancy when it comes to a deceased tenant's Will?**
 - A. It overrides the tenant's Will.**
 - B. It has no effect on the tenant's Will.**
 - C. It mandates division according to the Will.**
 - D. It invalidates the Will entirely.**
- 5. What component requires careful structuring in a buy-sell agreement?**
 - A. Ownership transfer policies**
 - B. Valuation clauses**
 - C. Taxation regulations**
 - D. Duration of the agreement**

- 6. What is a distinguishing feature of a QPRT in relation to gift tax exclusions?**
- A. It is eligible for the annual exclusion**
 - B. It generally results in a completed gift**
 - C. It is not eligible for the annual exclusion**
 - D. It can only be set up for 10 years**
- 7. Who typically is not eligible to inherit under intestate laws if there is no will?**
- A. Blood relatives**
 - B. Spouses**
 - C. Same-sex couples not blood related**
 - D. Adopted children**
- 8. What is the outcome of not including life insurance proceeds in the gross estate?**
- A. The estate may incur penalties**
 - B. The estate could face audits**
 - C. The estate may not benefit from the applicable credit**
 - D. The estate will not benefit from tax exclusion**
- 9. According to the Terminal Interest Rule, what must occur for property to be qualified?**
- A. The spouse must survive the condition**
 - B. The property must be equally divided**
 - C. The decedent must owe taxes on the property**
 - D. The property must be paid off completely**
- 10. Assets intended for charity upon death are treated in which way concerning the gross estate?**
- A. They are excluded from the gross estate.**
 - B. They are included but eligible for a charitable deduction.**
 - C. They are taxed at a higher rate.**
 - D. They must be reported separately.**

Answers

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- 1. B**
- 2. B**
- 3. B**
- 4. B**
- 5. B**
- 6. C**
- 7. C**
- 8. D**
- 9. A**
- 10. B**

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Explanations

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1. What happens if a parent dies before their child, according to the Predeceased Parent Rule for GSTT?

- A. The child must inherit nothing from the grandparent.**
- B. The child can inherit directly from the grandparent.**
- C. The child will only receive a limited inheritance.**
- D. The child inherits only if there is a will present.**

The Predeceased Parent Rule under the Generation-Skipping Transfer Tax (GSTT) provides that if a parent predeceases their child, the child can inherit directly from their grandparent, as if the parent were still alive. This is designed to ensure that the wealth passes down through the intended lineage without interruptions caused by the death of the parent. This rule is particularly relevant in the context of trusts and estate planning, where the goal often is to allow assets to skip generations without incurring additional taxation. The child steps into the position of the predeceased parent when determining inheritance rights, allowing the transfer of wealth to continue unobstructed. Therefore, the child is treated as though they were receiving the inheritance directly from the grandparent, ensuring that the estate plan reflects the wishes of the deceased grandparents regarding their legacy and the continuity of wealth through the family line.

2. In the net gift technique, what does the donee agree to do?

- A. Pay the estate tax**
- B. Pay the gift tax**
- C. Transfer assets to the donor**
- D. Exclude the gift from taxable income**

In the net gift technique, the donee agrees to pay the gift tax that is triggered by the transfer of the gift. This arrangement is often employed as part of estate planning strategies to manage tax liabilities associated with gifting assets. The primary rationale behind the net gift technique is to reduce the overall taxable estate of the donor while minimizing the impact of the gift tax burden. By having the donee (the recipient of the gift) assume the responsibility for paying the gift tax, the donor can effectively transfer more value without incurring immediate tax consequences for themselves. The donee benefits from the gift, even after accounting for the tax liability, which can still be a financially advantageous situation. The other options highlight various concepts related to estate and gift taxation, but they do not accurately describe the specific agreement made by the donee in the context of the net gift technique.

3. What is true regarding the treatment of real estate in a gross estate?

- A. It is always excluded from the gross estate**
- B. It includes worldwide real estate in the decedent's estate**
- C. Only property located in the state is included**
- D. Only commercial real estate qualifies for inclusion**

The treatment of real estate in a gross estate is accurately described by the assertion that it includes worldwide real estate in the decedent's estate. This is a fundamental principle in estate planning and tax law. When calculating the gross estate for estate tax purposes, all real property owned by the decedent at the time of death is included, regardless of its location. This means that if a person owned real estate in multiple countries, all of that property would be part of the gross estate, making it subject to the estate tax rules of the jurisdiction in question. Inclusion of worldwide real estate reflects the principle that an individual's estate consists of all assets they possess, irrespective of geographical limitations. This principle ensures a comprehensive assessment of the decedent's wealth, facilitating accurate estate tax evaluations and potential liabilities that may arise upon death. Understanding this concept is critical for estate planning professionals, as they must take into account all real property owned by a client, not just property located within the client's state of residence. Consequently, when advising clients on estate planning, it's essential to recognize the global nature of real estate ownership and its implications for estate taxation.

4. What is the implication of the joint tenancy when it comes to a deceased tenant's Will?

- A. It overrides the tenant's Will.**
- B. It has no effect on the tenant's Will.**
- C. It mandates division according to the Will.**
- D. It invalidates the Will entirely.**

The implication of joint tenancy in relation to a deceased tenant's Will is that it has no effect on the tenant's Will. In a joint tenancy, when one tenant passes away, their interest in the property automatically transfers to the surviving tenants due to the right of survivorship. This means that the deceased's portion does not become part of their estate and is not subject to distribution according to their Will. Thus, even if the tenant had made provisions in their Will regarding the distribution of their assets, those directives do not apply to property held in joint tenancy. The surviving tenants simply continue to own the property as before, which illustrates how joint tenancy operates independently of the deceased's Will. This characteristic of joint tenancy is significant for estate planning, as it ensures that certain assets can bypass the probate process entirely.

5. What component requires careful structuring in a buy-sell agreement?

- A. Ownership transfer policies**
- B. Valuation clauses**
- C. Taxation regulations**
- D. Duration of the agreement**

The component that requires careful structuring in a buy-sell agreement is valuation clauses. Valuation clauses are critical because they determine how the business will be valued when an ownership interest is sold, usually due to events like death, disability, or voluntary withdrawal of a partner. The valuation method needs to be clearly defined and agreed upon to ensure fairness and prevent disputes among current owners and their heirs. Having a well-structured valuation clause helps to set expectations and can involve methods such as fixed price, appraisal, or a formula based approach. If the valuation mechanism is ambiguous or not agreed upon, it can lead to disagreements at a sensitive time, potentially harming business continuity. Consequently, this aspect of a buy-sell agreement is vital for ensuring a smooth transition of ownership and proper pricing, thus reinforcing the stability of the business during ownership changes.

6. What is a distinguishing feature of a QPRT in relation to gift tax exclusions?

- A. It is eligible for the annual exclusion**
- B. It generally results in a completed gift**
- C. It is not eligible for the annual exclusion**
- D. It can only be set up for 10 years**

A Qualified Personal Residence Trust (QPRT) is a specific type of irrevocable trust that allows an individual to remove a personal residence or vacation home from their taxable estate while still retaining the right to live in the property for a specified number of years. The distinguishing feature of a QPRT is that it generally does not qualify for the annual gift tax exclusion because the person transferring the residence (the grantor) maintains an interest in the property during the trust term. Once the term of the QPRT ends and the grantor vacates the residence, the property passes to the beneficiaries, and at that point, the gift is completed. However, since the grantor retains an interest during the trust term, the gift is considered incomplete for the purposes of the annual exclusion, which is designed for gifts that are immediately given away without any conditions. This key feature differentiates it from other gifts that might qualify for the annual exclusion, making it relevant for understanding how such trusts work within the context of gift tax planning. The design and structure of a QPRT can provide significant tax advantages, but recognizing that it does not qualify for the annual exclusion is crucial for proper estate planning.

7. Who typically is not eligible to inherit under intestate laws if there is no will?

- A. Blood relatives**
- B. Spouses**
- C. Same-sex couples not blood related**
- D. Adopted children**

Under intestate laws, the distribution of a deceased person's estate is established by statutes that vary by state. Generally, individuals who are closely related to the decedent, such as blood relatives, spouses, and adopted children, are eligible to inherit under these laws. Same-sex couples who are not blood-related can be ineligible to inherit if they are not legally recognized as spouses or partners at the time of the decedent's death. In many jurisdictions, only legally married spouses and sometimes domestic partners have legal rights to inherit under intestacy laws. Therefore, a same-sex couple that does not have legally recognized status may not qualify for inheritance under intestate succession, resulting in option C being the correct choice. Blood relatives, spouses, and adopted children all have established rights under intestate succession laws. Blood relatives directly related to the deceased will typically be prioritized as heirs. Spouses, regardless of their gender, generally have strong inheritance rights. Adopted children are treated equally to biological children under intestate laws, meaning they have the same rights to inherit from their adoptive parents as biological children do. This ensures that all dependent family members, regardless of genetic ties, are adequately provided for under the law.

8. What is the outcome of not including life insurance proceeds in the gross estate?

- A. The estate may incur penalties**
- B. The estate could face audits**
- C. The estate may not benefit from the applicable credit**
- D. The estate will not benefit from tax exclusion**

When life insurance proceeds are excluded from the gross estate, it means that they are not counted towards the total value of the estate for tax purposes. This is significant because life insurance proceeds can be quite substantial, and their treatment can affect the tax burden of the estate. If these proceeds are not included in the gross estate, the estate misses out on the opportunity to benefit from the tax exclusion available for life insurance. Typically, life insurance proceeds payable to a named beneficiary are not included in the deceased's gross estate under certain conditions, but if the proceeds aren't managed appropriately, the estate could incur additional taxes. Other outcomes, such as incurring penalties or facing audits, generally relate to compliance issues rather than the treatment of life insurance proceeds specifically. The tax credit mentioned and the implications therein rely on proper estate management and inclusion of all necessary components in the gross estate, so excluding the life insurance does not maximize its potential benefits under tax law. Thus, the key outcome here is that the estate will not benefit from the exclusion, directly impacting the tax liability associated with the overall estate.

9. According to the Terminal Interest Rule, what must occur for property to be qualified?

- A. The spouse must survive the condition**
- B. The property must be equally divided**
- C. The decedent must owe taxes on the property**
- D. The property must be paid off completely**

The Terminal Interest Rule pertains to the treatment of property interests in the context of estate planning, particularly when considering the eligibility for certain tax benefits. Under this rule, for property to be qualified, it is essential that the spouse survives the conditions set forth in the estate plan. This means that the surviving spouse must have a continued interest in the property for it to be included in the marital deduction, which allows the property to pass to the surviving spouse without incurring estate taxes at the time of transfer. The reasoning behind this is rooted in the requirement that the transfer of property to a surviving spouse must be certain and not subject to potential loss due to conditions that could cause the property to revert back to the decedent's estate. As such, the survival of the spouse ensures that the property remains a transferable interest, thus qualifying for the tax benefits intended under the rule. The other options, while relevant to property and estate planning, do not address the specific requirement set by the Terminal Interest Rule for property to qualify in the context of taxation and marital benefits.

10. Assets intended for charity upon death are treated in which way concerning the gross estate?

- A. They are excluded from the gross estate.**
- B. They are included but eligible for a charitable deduction.**
- C. They are taxed at a higher rate.**
- D. They must be reported separately.**

Assets intended for charity upon death are included in the gross estate but are eligible for a charitable deduction. This means that while these assets are part of the total value of the deceased's estate for purposes of calculating estate tax liability, the estate can offset that value with the amount donated to charity. The rationale behind this treatment is that the government encourages charitable giving by allowing estates to deduct the value of charitable bequests when determining the taxable estate. This can significantly reduce the estate tax burden. By ensuring that these assets are included in the gross estate, the IRS can maintain an accurate assessment of the estate's total wealth before any deductions. In contrast, the other options suggest different treatments that do not align with tax laws regarding charitable donations upon death. Assets being excluded from the gross estate, taxed at a higher rate, or reported separately do not reflect the established principles governing estate planning and charitable contributions. Thus, the inclusion within the gross estate coupled with eligibility for a charitable deduction is the correct approach under the relevant tax regulations.