LIVING TRUSTS
AND
AVOIDING PROBATE

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Living Trusts and Avoiding Probate

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Chapter 1
Introduction

Estate Planning

In the broadest sense, estate planning is the process by which an individual prepares to dispose of his assets upon his death. This process, if done correctly, takes into account the laws of wills, taxes, insurance, property, and trusts. In this way, a person can take advantage of favorable laws while carrying out his or her wishes.

It is an individual's goals which should dictate the estate plan. In order to achieve an individual's estate planning goals, those assisting in the planning must understand not only the goals of the individual, but also the present financial circumstances of the individual and what strategies he or she is comfortable with. These strategies are the tools by which the goals are realized.

Estate Planning Background

Everyone knows someone who got rich the "old fashioned" way. They inherited it. Estate planning is as old as society. Pharaohs, kings, native peoples, and even peasants have always planned for their demise. It seems to be in human nature to take care of the ones we love in life and in death. People have gifted and passed along enormous amounts of wealth.

It makes sense then that the government would try to get its hands on this ongoing transfer of wealth. For example, 90 percent of the wealth in the U.S. is controlled by 5 percent of the population. These people are not spending all of this money before they die. This money is effectively kept from the rest of the population unless they get rich the other "old fashioned" way. They marry into it.

In order to get its hands on this money, the U.S. government began to tax inheritance in 1797. Later, in 1932, the U.S. government began to tax gifts made during an individual's lifetime. These laws have been modified over the years, but have existed in a form similar to what they are today since 1976.

These inheritance and gift tax laws can be quite complicated. It is the complicated nature of these rules that fuels the lucrative business that estate planning is today. Furthermore, it is unwise for an individual without a background in law, finance, or accounting to attempt to formulate an estate plan. In fact, the corner stone of almost any good estate plan should be a revocable trust, which must be prepared by a lawyer.

Estate planning is just too complicated and important to be attempted by someone without comprehensive education in the subject. Experience plays just as important a role. So, when a person is trying to decide on an attorney or financial planner to assist in estate planning, he or she should seek an individual who has knowledge and experience in that area.

Purpose of Estate Planning

The main objective in estate planning should be to dispose of an individual's assets according to his or her wishes. The plan can be enhanced by using planning techniques that pass along more assets or assets with a greater value. The use of a good estate plan can save thousands of dollars and add peace of mind. That peace of mind can be invaluable.

In addition to carrying out an individual's wishes, other goals of a good estate plan should be to avoid the probate court, unnecessary taxes, and unnecessary costs. These goals can be achieved by minimal expense at the planning stage. Without planning, these things are difficult, if not impossible, to avoid.

Again, while money is important. It is not always the most important thing. With estate planning, the client's goals and peace of mind come first. It just so happens that the primary concern for most people usually is saving money on taxes and fees. Occasionally, people want things done a certain way regardless of whether you have a better way (such as money making or money saving) to do it. In estate planning, your job is to carry out their wishes.

Living Trust as Part of an Estate Plan

Almost any good estate plan should incorporate a living trust (otherwise known as a revocable trust). A living trust is the most versatile tool an estate planner has at his or her disposal. Living trusts can help reduce taxes, reduce attorney's fees, give privacy and flexibility, and, most importantly, help avoid probate and guardianship.

In addition to making things easier at one's death, a living trust is a valuable tool if a person suffers incompetence or illness. Everyone knows they are going to die. They plan on it. What most people do not plan for is prolonged illness or senility. Unfortunately, one of the drawbacks of the wonderful advances we now have in medicine is that people are living longer. A longer life does not always mean a better one. Many people experience prolonged illness which can be expensive and trying on one's family. A living trust can alleviate many problems associated with prolonged illness and senility by spelling out who an individual wants to manage his or her affairs if he or she is not capable of doing so. This means that a living trust can help avoid expensive court proceedings called guardianships and keep people in their homes as long as feasibly possible. Most people would rather live at home than in a nursing home.

Living trust documents should be prepared by an attorney. Most types of property can be held in a trust and most property can be disposed of by a trust. The only drawbacks to a trust are the cost of having one prepared and the time it takes to re-title assets into the name of the trust. A living trust should usually be used as part of an estate plan.

The High Cost of Dying

Everything in today's world is expensive. So, why would dying be any different. Dozens of costs are associated with dying, among them: attorney's fees, court costs, filing fees, funeral costs, and taxes.

If an attorney is required to administer an estate, the fees could range from a couple hundred to tens of thousands of dollars. Attorney's fees vary depending on the size of the estate, the work involved, the litigation involved, and the experience of the attorney. Generally, the smaller the estate the less work involved and the lower the fee. But, there is no accounting for litigation. At $250 or more an hour, any litigation can be expensive. In some instances, the litigation can cost nearly the value of the estate.

Court costs vary depending on whether a probate estate needs to be opened. Probate fees are quite expensive considering that the court must oversee the administration of the entire estate from beginning to end. If no probate is required, that is there are no sole name assets, the court costs are minimal. The court fees consist of filing fees that most likely would not amount to more than a few hundred dollars.

The expression, “Only two things in life are certain, death and taxes,” rings true every day to those who deal with estate planning. Currently, an individual can gift $1.5 million during his or her life, or at his or her death, free of federal estate taxes. Anything over $1.5 million is taxed at a rate beginning around 40 percent and going up to around 60 percent. These numbers can be staggering if solid planning is not done.

For example, a single man dies leaving $2 million to his brother. After federal taxes, the brother receives $1.6 million. That is $400,000 in federal taxes.

This example does not take into account the state estate taxes. Most states do not want to miss out on this tremendous source of revenue. As such, states impose their own taxes. State estate taxes are not as high as federal taxes; however, they can be quite significant. About half the states have estate taxes and their rates can be as high as 20 percent.

Chapter 2
Probate and Guardianship

Probate is the court process by which the estate of a deceased individual is administered. This process involves collecting the individual's debts, paying necessary taxes, and distributing property to heirs and beneficiaries. This entire process is carried out by a court approved, or appointed, individual known as the administrator, executor, or personal representative of the estate. All of this is done under the supervision of the probate court.

The purpose of the probate procedure is to ensure that the decedent's wishes are carried out and that all debts are paid. Those debts include creditor's claims, distributions to beneficiaries, and taxes. It is the probate court that decides if things are being done correctly and when the estate is to be closed. While the probate judge does listen to the claims of those involved in the estate, and third parties, to make decisions the judge will also ask questions and oversee the process with a watchful eye.

A guardianship is the duty or authority of a guardian. It is also a legal arrangement under which one person has the legal right and duty to take care of another (the ward). This process involves a court proceeding by which the legal rights of an individual are taken away, such as the right to handle one's finances, and given to another individual to handle.

The purpose of a guardianship is to protect an individual who lacks the capacity to act on his or her own behalf. People who require guardianships are often people who are elderly and are suffering from severe dementia due to Alzheimer's disease or other illness. Some people may require a guardianship if they are physically handicapped, yet fine mentally. For example, a stroke victim may be unable to carry out everyday tasks and have no spouse to take care of them. It is also possible that an individual will recover from an illness and no longer require the guardian. While these instances are rare, another hearing is held to restore an individual's rights.

Guardianship and probate proceedings are similar in that the court is overseeing an individual who is acting in a representative capacity for another. That individual has to answer to the court for everything he or she does and every dollar he or she spends. These are not easy jobs. They are time consuming, emotionally draining, and expensive. They also can be avoided with good planning.

The Probate Process

Not all property held in an individual's name needs to be probated. In most states, the legislature sets a minimum amount, under which no probate is required. However, when you count all of the assets in an estate, it is usually over that limit. When the assets are below the amount set by the legislature, the court usually has some sort of summary proceeding that streamlines the process. When assets are over that statutory limit a formal proceeding is required.

The first step of the formal probate process is to open a probate estate. This means filing the papers required in the jurisdiction where the descendent resided. An attorney is highly recommended when opening a formal proceeding with the court. In some cases, an attorney is mandatory.

The court pleadings usually include a petition to open the estate, an order admitting the will to probate (if one exists), and a petition to appoint an executor or personal representative. The court requires the original will be filed, if one exists, because it is the document that expresses the decedent's wishes. The will should contain a statement of whom the descendent wants to serve as the executor or personal representative and who the beneficiaries are. If no will exists, an interested person, such as a spouse or family member, should petition the court to appoint the executor or personal representative. The court appoints the individual it believes will uphold the wishes of the decedent. At times, the court requires the executor or personal representative to post a bond, to ensure that the executor does not run off with the money. Upon the appointment of the executor or personal representative, that individual can begin the process of gathering or marshaling of all the assets.

Marshaling all of the decedent's assets can be a complicated process because it involves determining what the decedent owned at his death and under what legal title that property was held. Once the value, location, and legal title of the assets are determined, the person with the beneficial interest must be determined. It is the responsibility of the executor or personal representative to make sure all of the assets get to the correct individuals. This entire process can take a few months and sometimes several years. People have horror stories about going through mounds of papers looking for evidence of an insurance policy or a bank account a relative remembers might exist. This is why it is recommended that everyone make a list of all their assets and the account numbers associated with any accounts they have and place that list in their safe deposit box. It is always better to avoid problems than to deal with problems when they come up.

One of the most important elements of a probate administration is to make sure all creditors get paid. Creditor's claims and heirs must be paid before a probate estate can be closed. The executor or personal representative must notify the creditor's of an estate and the heirs that the estate has been opened. Once the creditor's have been notified, there is a limited amount of time for the creditors to make a claim. One of the main purposes of probate is to limit creditor's claims, so that creditors cannot come to the executor two years later and say the estate owes them money.

If a creditor files a claim against the estate, the executor or personal representative has two options.

- Pay the claim. With the payment, a release should be sent acknowledging payment and releasing the estate. The release should then be recorded with the court so the estate can be closed.
- Fight the claim. This option involves filing an objection to the claim with the court. The court battle can cost more than the claim, so the executor or personal representative must figure which will cost the estate more money.

After all claims have been settled and the tax liability has been determined, distributions must be made to the beneficiaries. After all distributions have been made, the executor or personal representative can begin closing out the estate. The executor or personal representative petitions the court to close the estate. The court must see the releases from all the creditors, the paperwork from the IRS and state taxing agency showing all tax liabilities have been paid, and receipts and releases from all the beneficiaries. The court will send a notice to the executor or personal representative that the estate has been closed. At this point, the executor or personal representative is released from all liability.

Disadvantages to Probate

The following are some of the disadvantages of probate:

- Cost is much higher than if assets are passed by means of a revocable trust
- Time administering the estate
- Court involvement
- Public nature of the probate proceeding

As you can see from the brief list above, judges and the probate process can be an enormous hassle. Why? Because, you are in court dealing with attorneys. Ask anyone who has ever been to court, they will tell you that it is expensive and it takes a long time to get anything accomplished. You are dealing with a system that is procedural and technical. The procedures need to be met with particularity in order to go forward.

Costs

While procedures are there to protect people's rights, they slow things down. During this time, you have an attorney on the clock. Attorneys are not inexpensive. These factors all combine with the emotional loss of a loved one and family disputes. This sounds more like a soap opera than a way to protect someone's interests.

The following are several examples of wealthy individuals whose estates were subject to probate.

Individual	Estate Value	Value After Probate*
Dwight D. Eisenhower	$2,905,857	$2,234,428
John D. Rockefeller, Sr.	$26,905,182	$9,780,194
Alta Rockefeller Prentice	$12,775,531	$4,103,216
Andrew Jergens	$5,891,781	$2,548,458
Elvis Presley	$10,165,434	$2,790,799
Orville Wright	$1,023,904	$772,261
J.P. Morgan	$17,121,480	$5,227,791
General George Patton	$844,364	$577,539
Marilyn Monroe	$819,176	$370,426
Franklin D. Roosevelt	$1,940,999	$1,366,132
Alwin Charles Ernst	$12,642,431	$5,518,319
Walt Disney	$23,004,851	$16,192,908
Frederick Vanderbilt	$76,838,530	$33,992,418
*These examples include the tax liability of the estates.		

Attorney's Fees

Attorneys do not work for free. In most states, a lawyer is required for probate. That attorney is going to charge fees. Those fees can range from 1 percent to 7 percent of the value of the estate. That fee can be a statutory percentage rate, set by the legislature, or it can be an hourly fee. Regardless of how the fee is calculated, it is usually going to be a significant portion of the estate.

The fees quoted by attorney at the beginning of an estate administration usually do not include litigation matters. Thus, if someone decides to contest the will, the litigation costs are in addition to the fee already quoted. This can drive the cost of a probate administration well above 10 percent of the value of the estate.

The problem with probate is that it makes the estate a matter of public record. This invites people to investigate the matter. Friends and family who feel slighted or left out are apt to cause trouble with the administration. Trouble comes in the form of lawsuits and litigation, and that costs money. That is money that could be saved if the estate never went to probate.

Here are some examples of attorney's fees associated with the probate estates of some famous wealthy people.

Individual	Estate Value	Attorney's Fees
Walt Disney	$23,004,851	$150,000
Nat King Cole	$1,876,648	$47,949
Harry Warner	$8,946,618	$50,000
Franklin Roosevelt	$1,940,000	$75,000
General George Patton	$844,364	$6,708
Orville Wright	$1,023,904	$20,360
Dwight Eisenhower	$2,905,857	$68,900

Executor's Fees

As already mentioned, it is a lot of work to administer an estate. The executor is entitled to a fee for the work done during the administration of the estate. That fee is usually set by statute and the executor can petition the court for more money if extraordinary work is required. The executor's fees can range from 2 percent to 4 percent of the estate.

Here are some examples of executor's fees associated with the probate estates of some famous wealthy people:

Individual	Estate Value	Executor's Fees
Walt Disney	$23,004,851	$125,000
Nat King Cole	$1,876,648	$22,946
Harry Warner	$8,946,618	$50,000
Franklin Roosevelt	$1,940,000	$325,000
General George Patton	$844,364	$6,048
Orville Wright	$1,023,904	$19,360
Dwight Eisenhower	$2,905,857	$30,500

Court Costs

The probate court must charge to pay for its existence. Judges make good livings and they do not do clerical work. So, the states and counties hire people to assist in the probate court. In most states, the fees for probate are statutory. The court simply charges the estate a percentage of its value. That percentage can range from 3 percent to 8 percent, depending on the size of the estate and the state in which the decedent died. Again, this fee is unnecessary if good planning is done and probate is avoided.

Time

Tempus fugit (*time flies*). Time flies when you have an attorney on the clock is more like it. Probate takes a long time. The best case scenario is six months. In some instances, a probate administration can last as long as two to three years. This is difficult for several reasons.

The length of time causes an emotional strain on a family. People always speak of closure and moving on after a loved one passes away. That is impossible when you are dealing with an ongoing court proceeding. The hardest hit is the surviving spouse who is usually acting as the executor or personal representative. The administration of the estate becomes a full-time job and can weigh on the surviving spouse’s mental state.

Similarly, the length of a probate can cause family problems beyond comprehension. Children, who tend to bicker already, have been known to stop speaking to one another or worse to sue each other. The stress of a probate procedure can wreak havoc on a family. These problems are often magnified when the children’s spouses get involved. While some of this may go on whether there is a probate or not, the chances are greatly increased because of the length of time and the open nature of the probate proceeding.

The family problems only get worse during the probate administration because assets cannot be distributed to beneficiaries until the estate is ready to be closed. Greed aside, when people are expecting to receive a considerable amount of money and it has been over a year since they were informed, they get restless. The anxiety over receiving their money creates distrust between the beneficiaries and the lawyer. People seem to think they are being lied too, manipulated, or even stolen from. This makes for a difficult situation for everyone involved. It also means that the beneficiaries are not getting the benefit of the decedent’s gift.

If it is not bad enough that the money can not be distributed to its intended beneficiaries, some courts have requirements that are even more strict. Probate courts can require that they approve of every dollar spent on the estate administration. Imagine having to petition the court for a year and a half every time the executor has to pay a bill the decedent owed. Imagine simple expenses, such as an electric bill, becoming a court proceeding. The length of the probate proceeding can be excruciating.

Real Estate

When an individual passes away owning real property in his or her individual name, that property becomes a probate asset.

Like other property, real property must be re-titled and distributed according to the wishes of the decedent. This can become complicated because the property is not always left to one person. When left to one person, the property goes to probate and after the court determines that everything is in order the executor or personal representative deeds the property to the beneficiary. When the property is left to more than one person, the process is the same except the property is deeded to multiple individuals. However, usually when more than one person inherits a piece of real estate they agree that, instead of fighting over who is going to use the property, they should sell it.

Property being sold from a probate administration is a hassle whether it was the decedent’s wishes or because the beneficiaries would rather have money. The length of the probate forces the beneficiaries to pay to keep the property up. This can be expensive, especially with an older home. In addition, the taxes and the mortgage must be paid as well. All of these costs mount up before the beneficiaries have received a cent of their inheritance. You can imagine the cost of trying to pay all the bills for that big old house you grew up in or the lovely beachfront condo your parents retired in.

Probate in Different States with Real Property

As discussed earlier, when an individual dies with a piece of real property in his sole name, a probate is required to transfer that asset. When an individual dies with property in more than one state, a probate has to be opened in each state in which each piece of real property is located.

Many people who are not considered wealthy by any standard have summer homes or condos in vacation spots. For example, people may own a home in New York and buy a condo in Florida. When they retire, they sell the home in New York and move into the condo in Florida. Then they buy a place in North Carolina to go to in the summer because it is too darn hot to be in Florida in the summer. When these people die, their kids have to deal with probate courts in Florida and in North Carolina. This most likely means two lawyers, because lawyers need to be licensed in every state in which they practice. So, unless they find an attorney licensed in all the states in which the decedent owned property, they will need more than one attorney. Of course, that means twice the expense. Similarly, court costs increase and the possibility of incurring another state estate tax court can cost the estate much more money.

Guardianship is Similar to Probate

A guardianship can be similar to probate. The court is overseeing the guarding as he takes care of the ward. The ward is the individual who has been declared incapacitated. This is like the executor having to answer to the court for everything done for the decedent. The court is simply looking out for the rights of an individual who cannot stand up for himself.

Expense and Time

A guardianship is extremely expensive because the guardian needs to be appointed. The appointment of a guardian involves a lengthy court process by which the court terminates the rights of the incapacitated individual and places those duties in the hands of the guardian. In essence, this is like a trial. That means attorneys fees and court costs. Once the guardian is appointed, the fees do not stop. The guardian is paid a fee for handling the ward’s affairs. Additionally, the guardian must continually inform the court of the ward’s finances. The guardianship can continue indefinitely—that is until the ward passes away. A guardianship is likely to cost several thousand dollars initially and about 5 percent of the wards assets annually in guardian and accounting fees.

Appointed Guardian

The court usually appoints a relative to be a guardian; this makes sense because relatives are the people the court can trust most to take care of an individual. However, this can place an enormous strain on a family when other family members begin to second guess the guardian about what is right for the incapacitated individual. In most cases it is probably preferable to the alternative, which is that someone not related to the ward be appointed guardian. In some instances, however, the court must appoint a non-family member if the incapacitated person has no family or no family capable of acting. Most people’s worst fear is being alone, confused, and looked after by a complete stranger who has no idea what their wishes were.

Accounting Every Year

A guardianship requires an accounting every year. That means that the guardian needs to hire an accountant to file a formal accounting statement with the court. The accounting statement needs to include every dollar spent during the year. This is tedious and expensive.

Chapter 3
Assets Subject to Probate and Guardianships

Simply put, almost any asset owned in an individual's sole name is subject to probate and guardianship.

Bank Accounts

Bank accounts owned in an individual's sole name are subject to probate and guardianship. In some states, even assets owned jointly with another individual are subject to probate because they do not presume the right of survivorship. Rights of survivorship means that when one person dies the account automatically transfers to the other party. So, it is important that even bank accounts that are jointly held be placed in a revocable trust or have the right of survivorship specifically designated. Bank accounts that have beneficiary designations such as F/B/O (for benefit of), POD (pay on death), and Totten accounts do avoid probate.

Brokerage Accounts

Brokerage accounts follow the same rules as bank accounts and, as such, do not avoid probate or guardianship unless a beneficiary is designated or a joint owner has survivorship rights. However, many brokerage accounts do not offer beneficiary designations.

Life Insurance and Annuities

Life insurance policies only avoid probate if a beneficiary is designated. It is important that a secondary beneficiary be designated in case the primary beneficiary passes away. If the primary beneficiary is deceased at the time the insured dies, a probate must be opened.

IRA and 401k Accounts

Individual retirement accounts are subject to probate if a beneficiary is not designated or the beneficiary designated is not living and a secondary beneficiary is not named. The IRS has distribution rules and rollover provisions for spouses when a beneficiary is designated. But, those rules do not do much good when a beneficiary is not designated.

Individual Stocks

Stocks are property and when someone dies owning a stock in his or her individual name it becomes a probate asset. There are ways to avoid a stock becoming a probate asset though. The best way would be to own it in the name of a revocable trust. Another way, the stock could be owned jointly with survivorship rights.

Government Notes and Bonds

Like all of the assets discussed, notes and bonds are probate assets if owned in an individual's name at the time of their death. The only ways to avoid the notes and bonds being probated are:

- Place them in a revocable trust
- Own them jointly with another individual with survivorship rights
- Designate a beneficiary upon death

Real Estate

Real property is subject to probate in the state in which the decedent owned it, in his sole name, at the time of his death. Probate can be avoided by:

- Placing the property in a revocable trust
- Owning it jointly with someone who has survivorship rights
- Transferring the ownership to an individual or irrevocable trust that allows him to live out his days on the property

These may or may not be recommended alternatives to the trust and should be reviewed before changing the title on the property.

Case Studies

Case 1

Husband and wife have been married for 25 years. They have retired to Florida, from New York, and have approximately $1 million in assets. The assets consist of a home in Florida worth $250,000 (owned in wife's revocable trust), two brokerage accounts worth $250,000 each (owned in each spouse's revocable trust), and a joint checking account worth $250,000.

Unfortunately, husband has a heart attack and dies. His revocable trust left everything to his wife. Wife consults with attorney. Attorney informs wife that all that needs to be done is to re-title the joint checking account into the name of her revocable trust and to contact the brokerage firm and notify them that her husband is deceased and that she is the sole beneficiary. As sole beneficiary, the brokerage account can be re-titled into the name of her trust. The attorney charges $1,000 for the consultation and agrees to assist in the re-titling by helping to fill out forms and answer questions.

Three months later everything has been resolved and the wife went through almost no additional stress during the process.

Case 2

Husband and wife have been married for 25 years. They have retired to Florida, from New York, and have approximately $1 million in assets. The assets consist of a home in Florida worth $250,000 (owned jointly), two brokerage accounts worth $250,000 each (owned in each spouse's sole name), and a joint checking account worth $250,000.

Unfortunately, husband has a heart attack and dies. He had a will that left everything he owned to his wife. His wife hires an attorney to handle the estate. The attorney informs the wife that they will have to open a probate for the assets that her husband owned in his sole name. Attorney's fee for the probate is $5,000 or 2 percent of the probate estate, which is $250,000. The attorney also informs the wife that there will be various court costs associated with the probate administration, which will total several hundred dollars (significantly less than if her husband had died in most other states). Finally, the attorney informs the wife that she needs to re-title the joint checking account into the name of a revocable trust to avoid a probate when she passes away.

Nine months later the probate court closes the probate. The wife has dealt with over $5,000 worth of unnecessary costs, having $250,000 worth of assets tied up for six additional months, and all the stress that comes along with her husband's death.

Case 3

Husband and wife have been married for 25 years. They have retired to Florida, from New York, and have approximately $1 million in assets. The assets consist of a home in Florida worth $250,000 (owned jointly), two brokerage accounts worth $250,000 each (owned in each spouse's sole name), and a joint checking account worth $250,000.

Unfortunately, the husband and wife die in a car accident. Both had wills that left everything to their only son. The son lives in New York. The son flies down from New York and meets with the attorney. The attorney informs the son that all of his parent's assets have to be probated. The attorney's fee for the probate is $20,000 or 2 percent of $1 million. The attorney also informs the son that the court will likely require a $25,000 bond, because he is not a Florida resident. Additionally, the attorney informs the son that various court costs are associated with the probate administration, which will total several hundred dollars (significantly less than if the husband and wife had died in most other states). Finally, attorney informs the son that he will have to petition the court to sell his parent's home and that it could take several months to get approval.

Twelve months later the probate court closes the probate. The son has dealt with the loss of both his parents, the sale of a home, and an arduous court proceeding. Revocable trusts would have prevented so many costs and saved so much time and emotional strain for the son.

These three case studies show how expensive and time consuming a probate can be. Nonetheless, the cases cannot illustrate the emotional strain a probate proceeding can place on the survivors.

Simultaneous Death

Case 3 shows why joint ownership is not a substitute for a trust. Joint ownership does not avoid the problem of simultaneous death. The reason joint ownership avoids probate when one spouse dies is that someone has survivorship rights. When both spouses die at the same time there is no survivor. The common disaster, as it is often referred to, is a contingency that most people do not account for. The living trust is the best way to plan for a common disaster.

A common disaster is not the only way that joint ownership can result in probate. Another example is when one spouse dies and the other dies soon after. If the surviving spouse has not re-titled the asset in the name of the trust or designated a beneficiary, a probate will be required. The living trust is the best way to take care of of these problems all at once.

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Chapter 4
How to Avoid Probate With the Living Trust

A living trust is a separate legal entity from the individual creating it. More specifically, a living trust is a legal document. The living trust is created by an individual, controlled by the same individual, all while that individual is the beneficiary of the trust. Assets are placed in a trust by titling them in the name of the trust. The trustee controls those assets according to the terms of the trust. Assets in a trust are not subject to probate because they are not owned by the individual, only controlled by the individual, who just happens to be the beneficiary of the trust.

The living trust can hold any property you wish to place in it. Some states require certain language to be in a trust to hold certain types of property. For example, some states require specific language for a trust to hold subchapter "S" stock. Regardless, if you have property you want to place in a trust, you can do so.

The living trust is also known by other names, such as revocable trust and family trust. Living trusts are also used to create other trusts. Some of the trusts created by living trusts are:

- Residuary trusts
- Marital share trusts
- QTIP trusts
- Spendthrift trusts
- Irrevocable trust

Discussion of all these trusts is beyond the realm of this forum, but it is important to understand that these trusts exist to differentiate them from living trusts.

How it Works

Once the living trust is "funded" (that is, the assets are placed in it) there is next to nothing to do. The trust assets are treated as though you own them. An individual can borrow against the assets in the trust, sell them, transfer them, or even gift them away. That is the great thing about a living trust—flexibility. The living trust has no drawbacks aside from the work that needs to be done when it is created to title assets in the name of the trust.

Common Misconceptions About Living Trusts

Many people have misconceptions about living trusts. Some of the misconceptions are:

- With a will assets will not have to go through probate
- A trust is not needed if assets are valued at under a million dollars
- A living trust can be used to avoid creditors
- A living trust shelters assets in case of the need for long term care

These misconceptions can lead to angry clients when circumstances arise in the future. It is important to explain to clients that these misconceptions are false so they do not plan according to bad information and so they cannot come back later and claim that you misled them.

Will Does Not Go Through Probate

Many people think that if they die with a will no probate is needed. That is incorrect. A will is a set of instructions telling the court on how to proceed with the probate administration.

A will only tells the probate court where you want your assets to go when you die. A will prevents assets from being subject to the state's intestacy statute. Those assets will still go through the probate court.

Under $1.5 Million, Trust Not Needed

The federal government allows individuals to gift up to $1.5 million, tax free, throughout their lifetime or at death. This is called the unified tax credit and it is set by statute. It will be going up over the next few years. However, this has nothing to do with the transferring of your assets through probate.

Year	Unified Credit/Exclusion Equivalent
2002-2003	$1 million
2004-2005	$1.5 million
2006-2008	$2 million
2009	$3.5 million
2010 and beyond	No Estate Tax

In *Chapter 7 Essential Provisions in Trust,* the AB Trust is explained. Under the AB Trust, a married couple with over $1.5 million can maximize their unified tax credit by creating two revocable trusts and funding them by placing half of the assets in one trust and half in the other. Upon the death of either spouse, their trust will create a residuary trust, which is irrevocable, for the benefit of the surviving spouse during his or her life and someone else after his or her death. By doing this, when the surviving spouse passes away he or she will only be passing on half of his or her assets in the IRS's eyes, because the assets in the irrevocable residuary trust have already been passed on by the first spouse to die. The first spouse to die used his or her unified credit and now the second spouse to die has used his or her unified credit.

Set Up a Trust to Avoid Creditors

The greatest misconception about a living trust is that affords protection against creditors. Assets in a living trust are treated as though they are owned by the trustee because the trustee in a living trust is the settlor, trustee, and beneficiary. In laymen's terms, the trustee "owns" the trust assets and can do whatever the trustee wants to do with them. The only ways to avoid this would be to make the trust irrevocable with someone other than the settlor as the trustee. This would defeat two of the main purposes of the trust—flexibility and control.

Creditor protection is much too complicated to be discussed along with a living trust. However, to end the confusion, a living trust does not give an individual any protection against creditors.

No Protection in the Event of Long Term Care

A revocable trust does not provide protection from creditors. Similarly, having all of your money in a revocable trust will not qualify you for Medicaid. As discussed earlier, a settlor has control of the assets in a revocable trust and can do as the settlor chooses with them. These are considered assets for Medicaid purposes. The assets in a revocable trust can be attached by the provider of long term healthcare.

People confuse revocable trusts with irrevocable trusts with regards to long term healthcare. Irrevocable trusts do not provide asset protection from a provider of long term healthcare, unless the transfer to the trust was made over five years before the healthcare begins. Regardless, if you need to enter a long term healthcare facility and you have assets in a revocable trust, those assets can be attached.

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Chapter 5
Parties to the Trust

To be effective, a trust must include several essential parties:

- Settlor or Grantor – the individual who creates the trust
- Trustee – individual who administers the trust
- Beneficiary – Individual to whom the trust or the assets in the trust will pass according to state intestacy law or worse, escheat to the state

Assets that escheat to the state are assets that do not pass to any lineal heirs and pass to the state because no one has a legal claim to them. That is the worst case scenario.

In addition to the parties mentioned above, every trust should list a successor trustee and an alternate to ensure that an individual the settlor trusts can administer the trust if or when the settlor passes away.

Settlor or Grantor

The settlor of a trust is the individual who creates the trust. The settlor is also referred to as the grantor. In a living trust, the settlor usually acts as the trustee. This is done because the settlor wants to control the assets placed in the trust. The assets in a revocable trust will be treated as though they are the property of the settlor. As such, the settlor can do whatever the settlor wishes with the assets placed in the trust.

The settlor is the individual who funds the trust. Funding the trust is the process by which the settlor re-titles assets from his or her sole name into the name of the revocable trust. It is important to fund the trust because assets not placed in the trust must be probated.

Trustee

The trustee is the individual or corporate fiduciary that controls the assets in a trust and carries out the terms of the trust. Legal title for the assets in the trust is vested in the trustee. The trustee, in a living trust, can do whatever he or she desires with the trust assets; such as paying bills and making gifts. A trustee basically acts as the owner of the assets in a living trust.

Trustees of irrevocable trusts and revocable trusts with beneficiaries other than the trustee must act according to the express wishes of the settlor. As such, the trustee of an irrevocable trust may not be able to pay personal bills or make gifts of money, unless the trust specifically states that the trustee is allowed to do so. Irrevocable trusts do not afford the flexibility a living trust does.

It is possible to have more than one trustee for a trust. When more than one trustee is named, state law usually requires the signature of all trustees for all transactions involving trust assets. However, since a living trust is a flexible document, the trust can be set up so trustees can act independently of one another. Regardless of whether this is a good idea, it shows how a living trust can be written to accommodate a variety of circumstances.

Beneficiary

A beneficiary is an individual or organization that stands to benefit from a trust. A beneficiary can be:

- Current
- Contingent
- Specific
- Income
- Remainder

A current beneficiary is receiving the benefits of a trust currently. Distributions are made to that person from the trust by the trustee. In a living trust, until the death of the trustee, the trustee is the current beneficiary and as such spends money from the trust for the trustee's benefit.

A contingent beneficiary is an individual or organization that stands to benefit from a trust if a certain set of circumstances, spelled out in the trust document, occur. However, in a living trust, contingent beneficiaries are rare and when they do exist they usually only stand to benefit from the trust after the settlor's death and some other specified event.

A specific bequest beneficiary is an individual or organization that the settlor designated a certain dollar amount to be given to upon his or her death. Specific bequests get paid before all other beneficiaries at the death of the settlor.

An income beneficiary is an individual or organization that receives the income from a trust but not the trust assets themselves. These types of beneficiaries usually only exist in irrevocable residuary trusts where a surviving spouse receives income from the residuary trust but does not invade the principal. This is done for tax purposes.

A remainder beneficiary is an individual or organization that stands to benefit from a trust after all specific bequests have been made. The remainder beneficiary receives everything that is left over (the rest, residue, and remainder) after all specific bequests have been made. In a living trust, remainder beneficiaries only exist after the settlor has passed away.

Successor Trustees and Alternates

A successor trustee is the individual or corporate fiduciary that takes care of trust assets and distributions when the trustee becomes unable or unwilling to act. The successor trustee usually takes over after the death of the trustee, but at times the successor trustee takes over after the trustee becomes ill or is declared incompetent.

The successor trustee is named in the trust document. It is usually recommended that a family member be named, but in some instances it is better to have a corporate fiduciary. Choosing the successor trustee is very important because the successor trustee is the person who is supposed to make sure that the settlor's intent is carried out after he or she has died or is unable to act himself or herself. If the right person is not chosen, then the entire purpose of the trust can be frustrated. The following chart shows the advantages and drawbacks of having a family member or corporate fiduciary serve as successor trustee.

Benefits of Family Member as Successor Trustee	Drawbacks of Family Member as Successor Trustee
1. Knowledge of decedent	1. Family pressure
2. Close to family (easy to get information)	2. Can be a full-time job (great responsibility)
3. Trustee's fee goes to a family member	3. Lack of knowledge of the system
4. Cheaper than corporate fiduciary	4. Family members upset they were not chosen to act

Benefits of Corporate Fiduciary as Successor Trustee	Drawbacks of Corporate Fiduciary as Successor Trustee
1. Knowledge of the system	1. Expensive
2. No ties to family (no family pressure)	2. Does not know family
3. Accountable	3. Detached and unresponsive

As you can see, picking a successor trustee is difficult. It is just as difficult to decide on an alternate. An alternate should be selected in case the person you chose is unable or unwilling to act. The same analysis should be used to pick an alternate as was used to pick the successor trustee. Usually, the alternate is someone who is younger than the successor trustee because it is less likely that he or she would have passed away. Regardless, if the named successor trustee passes away while the settlor is still alive it is recommended that the trust be amended to name a new successor trustee.

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Chapter 6
Allocation and Distribution of Trust

How to List Beneficiaries

A trust should list the current beneficiaries first. The revocable trust should spell out that the settlor has the right to use trust assets for whatever the settlor chooses. This way, when the trust is read, it is clear that the settlor is a beneficiary. Once the trust lists the current beneficiaries, the trust should then list the beneficiaries that will receive money at death.

- First listed should be the specific bequest beneficiaries. Since the specific bequests will be distributed before any residuary assets, the specific bequest beneficiaries should be listed before residuary or contingent beneficiaries.
- Finally, the residuary beneficiaries should be listed last. The residuary beneficiaries are the beneficiaries who divide the remaining assets after specific bequests have been distributed.

It is also important to make sure that all beneficiaries' names are spelled correctly. This seems obvious, but many people spell common names different ways. Beneficiaries that have the same name as another individual need to be distinguished from one another. For instance, John Doe might have a son named Jack Doe and a cousin named Jack Doe. Simple problems like this can be solved by using descriptive terms like "son" or "cousin."

Choosing beneficiaries is a very personal thing. It is no one's place to tell someone how he should distribute his assets upon his death. It is not even his spouse's business, unless he chooses to make it his spouse's business. Many spouses do their estate planning together and leave their assets depending on what the other spouse has planned. This can cause problems in making up a trust, especially with second marriages. People usually want their assets to go their children. When the spouses have different children it presents a problem because each spouse wants his or her children to receive the assets upon the demise of the other. Each of these spouses should make his or her trusts according to his or her wishes and not his or her spouse's wishes.

Per Stirpes Versus Per Capita

Per stirpes is a Latin phrase that means, "By roots or stocks; by representation." It is used in estate planning to describe how a class of beneficiaries will take a decedent's share of assets. When an individual directs his or her assets to be distributed to an individual if living, otherwise, per stirpes, the assets will be passed along to the individual unless that beneficiary is not living. If that beneficiary is deceased, the assets will pass to the next generation along the beneficiary's bloodline and be divided amongst those individuals.

For example: John Doe creates a trust leaving all of his assets to his daughter Jane Doe if living, otherwise, to her issue per stirpes. John Doe passes away. Unfortunately, Jane Doe died one week earlier while John Doe lay incapacitated dying in the hospital. Jane Doe had three children, James Doe, Jack Doe, and Janet Doe. John Doe's assets will pass to James, Jack and Janet in equal shares, as they are Jane's issue. Janet had a brother named Jerome who had not spoken with his father, John, in many years. Jerome received no share of the assets because they were distributed per stirpes along Jane's bloodline. Note that even if James, Jack, and Janet had all passed away prior to John's demise, Jerome would still not receive any of the assets. The assets would pass to the children of James, Jack, and Janet in equal shares.

Per capita is a Latin phrase that means, "By the heads or polls; according to the number of individuals; share and share alike." It is used in estate planning to describe how a class of beneficiaries will take a decedent's share of assets. When an individual directs his or her assets to be distributed to an individual if living, otherwise, per capita, the assets will be passed along to that individual unless that beneficiary is not living. If that individual is deceased, the assets will be passed on in equal shares to the other beneficiaries in that group or class.

For example: John Doe creates a revocable trust leaving all of his assets to his two children Jane Doe and Jerome Doe if living, otherwise, to the survivor of the two per capita. John Doe passes away. Unfortunately, Jane Doe died one week earlier while John Doe lay incapacitated dying in the hospital. Jane Doe had three children, James Doe, Jack Doe, and Janet Doe. James, Jack, and Janet are minors, have no father and are in dire need of money. Regardless, they will receive none of the assets because the assets pass per capita to beneficiaries listed. When you have two beneficiaries and one dies, the other beneficiary will receive all of the assets.

The descriptions of the per stirpes method of distribution and the per capita method of distribution should illustrate the importance of planning. It is important to decide how you would like your assets distributed if your beneficiaries are not alive when you pass away. Under the per stirpes method, the children or legal heirs of a beneficiary will receive the assets left to that beneficiary. Under the per capita method of distribution, the other beneficiaries will receive the assets left to that beneficiary. The results vary greatly depending on which method you choose.

The decision on what method to use should be based on where you want the assets to go. Many times people do not choose the per capita method because under that method the beneficiary is already receiving assets. In short, they do not wish to leave out part of the family just because their mother or father passed away. The per stirpes method keeps assets going to the children of your child, even if they predecease you. This is important when the children need the money, so they can be taken care of. Other people only wish to leave money to their own children and not their grandchildren. They take the position that it is their parents' responsibility to look after them. It is also possible that certain beneficiaries are better off than others and their children do not need the money as much as a named beneficiary.

Rule From the Grave Provisions to Protect Assets

In some circumstances, people have requirements for special provisions. These can be handled in the following ways.

Issues With Second Marriages

Second marriages are common and they present unique problems for estate planners. Many people in second marriages enter them with children from their first marriage. This creates a problem because the way most people distribute their assets upon their death is to leave everything to the surviving spouse. Since the surviving spouse is not the parent of the deceased spouse's children there is no way to be certain that the assets left to the surviving spouse will pass to the deceased spouse's children. A revocable trust can assure that the assets end up in the hands of the deceased spouse's children and not the children of the surviving spouse.

A revocable trust can be set up to create an irrevocable trust upon the settlor's death. The irrevocable trust is set up to pay income to the settlor's surviving spouse during his or her lifetime. Upon the death of the surviving spouse, the trust can be set up to distribute the residuary to the settlor's children.

Another way to make sure that assets go where you want them to go after you pass away and you are in a second marriage is to sign a prenuptial or postnuptial agreement. A pre-nupt can specifically delineate what assets belong to each spouse, so upon either demise or divorce the assets can be distributed accordingly. It is important to know that certain states do not enforce pre-nupts or allow you to disinherit your spouse. So, all the planning in the world will not help you if you die a resident of one of those states. The lesson to be learned is to know the laws of the state in which you are a resident and plan accordingly or move to a state that has rules that suit you.

Disinheriting a Child

People often disagree with the choices their children make or the way they live their lives. Some people go as far as to carry those disagreements with them to the grave. People disinherit their children. In every state it is possible to disinherit children over 18. A child can be disinherited by simply omitting the child's name from the list of beneficiaries, but this will leave the estate open to the possibility of a lawsuit. A child can still make a claim that his omission from the list of beneficiaries was a mistake and thus will still have a legal right to a share of the assets. A better way to disinherit a child is to specifically state in your revocable trust that it is your intent to disinherit your child.

Specific Bequest, Leaving Specific Assets

A specific bequest is a specific asset or amount of money that is left to an individual or charitable organization in a will or trust. With regards to a trust, upon the death of the settlor the specific bequest is paid out before other trust distributions. If the individual to receive the specific bequest is not living, the gift will lapse and be distributed as part of the residue, unless the settlor includes a provision designating where the money should go upon his death.

Many people make specific bequests of personal items like jewelry or art work. In some states, these things do not need to be placed in a trust, because the law allows personal effects to be gifted outside of probate. However, when these items are worth a considerable amount of money, it is advisable to title the ownership of them in the name of the trust. Then, you can make specific bequests of them to assure they pass to the intended beneficiary. People also make specific bequests of their home. Many people like to keep their home in their family and not have it sold upon their death. A home will pass to the specific beneficiary as designated unless state law interferes. In some states, the Homestead law could prevent a specific bequest of qualified homestead property when the decedent has a spouse or a minor child. Laws like this are designed with similar intent to laws that prevent decedents from disinheriting their spouses. Therefore, it is important to understand the jurisdictional laws so your estate plan is not thwarted.

It is important to understand that if an estate does not have enough money to pay the specific bequests, the residuary beneficiaries will get nothing. So, when making a trust, a settlor needs to carefully and realistically contemplate how many assets he will possess at his demise.

People often have far more in their estate than they planned for. Assets appreciate at a considerable rate when you leave them invested for 20 or 30 years without touching them. Also, property values can double or even triple in 30 years time. These things need to be considered when you leave the gift of your home to an individual, who likely will own his or her own home at the time of your death and will likely sell your home.

Residuary, Percentages

The residuary of an estate is all of the assets that are left over after all specific bequests have been made. A residuary beneficiary is a beneficiary who stands to receive the residue of a trust. There may be more than one residuary beneficiary and those beneficiaries can receive the residue in equal or unequal shares depending on the settlor’s instructions. The residue of an estate is usually divided by percentages because it is almost impossible to determine the exact amount of the residue of an estate when the revocable trust is created. It is difficult to determine the residue of a trust because assets appreciate and depreciate over time. So, the residuary beneficiaries usually receive a percentage of the residue of a trust.

As discussed with specific bequests, specific bequests are paid before residuary beneficiaries receive any assets. If no assets remain after specific bequests are paid, the residuary beneficiaries will receive nothing.

It is important for the settlor to determine how the residuary assets are to be distributed if a residuary beneficiary is deceased. The assets could be split between the other residuary beneficiaries or the assets could pass to the heirs of the deceased residuary beneficiary. This is an important decision for a settlor to make. It is also important for the settlor not to forget to designate where the residue of the trust is to go. If no residuary beneficiary is listed, the residuary assets must be probated. They must be probated because they do not vest in a beneficiary. They will go through the probate court and will be distributed according to the jurisdictions intestacy statute (the statute used when someone dies without a will). This is obviously not the intent of the settlor so it is important to always include a clause in the revocable trust distributing the residue.

Successor Trustee Distribution of Assets

Revocable trusts often contain provisions that direct that the successor trustee to simply distribute assets amongst beneficiaries. Under this type of distribution scheme the successor trustee will determine the value of trust assets and divide them as is to the beneficiaries. This method enables the successor trustee to transfer assets without having to endure the burden of selling off assets like a piece of property. The sale of a piece of property can be time consuming and if done hastily can result in a financial loss. Similarly, stocks and other assets may not be easily sold. The drawback to this type of distribution is that the assets may not be easily divided among beneficiaries.

Imagine that Mary passes away with two assets in her trust and two beneficiaries listed to split the assets. The two assets are a home worth $400,000 and a brokerage account worth $100,000. Under the provision of Mary's trust that states to simply distribute assets between the beneficiaries, so the home must be sold because the other asset is not worth enough to distribute as a like kind asset.

A revocable trust can also contain a provision that states that the successor trustee must sell all of the assets upon the death of the settlor and distribute to the beneficiaries in their designated shares. This provision will force the successor trustee to endure the burden of selling all of the trusts assets, accounting for the value of each asset to the beneficiaries and distribute the proceeds to the beneficiaries as the trust directs. While this seems like a hassle, it may be easier for the trustee than attempting to distribute assets and make the math work on the value of the assets distributed.

Under the current tax laws, the estate of an individual receives a stepped up basis for tax purposes. That means that assets are valued at their fair market value at the time of death of the decedent. This means that the estate is not liable for the capital gains on stock that has appreciated between the time the stock was purchased by the decedent and the time of death. The current tax law enables the successor trustee to sell assets without making the estate liable for tremendous capital gains.

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Chapter 7
Essential Provisions in Trust

Spendthrift Provision

A spendthrift provision is a clause placed in a trust that protects assets from the creditors of beneficiaries. This provision makes the beneficiary's interest in the trust inalienable and unassignable. It is essential that this provision be placed in trusts because, otherwise, assets in a trust will be vulnerable to judgments and liens of a beneficiary's creditors. The beneficiaries of a trust are usually the settlor's children and grandchildren. Children and grandchildren are often irresponsible and careless. Some children are more responsible than others, which may cause a settlor to create a trust for the benefit of an irresponsible or young child upon the death of the settlor. These trusts hold assets for the benefit of a beneficiary and, if set up correctly, can provide further protection from creditors. The settlor should realize that even if beneficiaries are responsible, hard times may come along and bring financial difficulties so planning should be done to protect assets from creditors.

As an example, John Jr. is the beneficiary of John Sr.'s trust. John Jr. likes to gamble and has extreme financial problems. He has creditors hounding him day and night for gambling debts. John Jr. pledges his interest in John Sr.'s trust as security for a loan to pay off his gambling debts. Fortunately, John Sr.'s trust contains a spendthrift provision which prevents the provider of the loan from attaching any of the trust assets. John Jr.'s creditors have no claim to the assets of John Sr.'s trust until John Jr. actually takes possession of the assets. Once John Jr. takes possession of the trust assets they belong to him and his creditors can attach liens and judgments against them. It would be wise in this circumstance for John Sr. to amend his trust to provide that the assets that will pass to John Jr. at his death be held in trust for his maintenance and support. As long as John Jr. is not the trustee of that trust, the assets cannot be attached by John Jr.'s creditors.

It is important to note that a few states do not enforce spendthrift provisions. So, it is important to know the laws of the state in which you create the revocable trust and where you reside. Most states do, however, enforce these provisions so it is important that a spendthrift provision is placed in your revocable trust.

Right to Income

Revocable trusts should contain a provision that states that the settlor has the right to all the income generated from trust assets. One of the greatest attributes of a revocable trust is the control the settlor maintains of the assets he or she placed in the trust. Along with that control of trust assets, a settlor should also receive the benefits of the assets placed in the trust, namely the income generated by the assets in the trust. A revocable trust would lose a great deal of its luster if the settlor could not spend the interest gained on investments placed in a revocable trust. The ability to receive income generated from the trust should be enumerated in the trust.

A settlor may also wish to consider a right to income clause with respect to his surviving spouse or children. Many people create what are known as residuary trusts and marital share trusts. These trusts are created for estate tax planning purposes and usually include right to income clauses. Under these types of trusts, a surviving spouse is the successor trustee of an irrevocable trust set up for his or her benefit. Their children are the residuary beneficiaries of the trust and the surviving spouse is the income beneficiary. That means that the surviving spouse will receive the income generated by the trust assets and upon his or her death the beneficiaries will receive the residual assets.

Powers Clause

Every trust should enumerate the powers vested in the trustee and the successor trustees. In a revocable trust, the settlor is the trustee so the trust should make the powers of the trustee as broad as possible. For instance, a revocable trust should spell out that the trustee can borrow against trust assets, buy and sell real property, and spend trust assets for the benefit of the settlor. Rarely, if ever, will a settlor wish to limit his or her power with regards to his or her revocable trust. But, in the rare case that they do, it should be clear in the trust how the power is limited.

It is also advisable that the trust enumerate specific powers that may not be standard. A settlor may like to buy and sell stock on margin. This power should be spelled out because many brokerage firms are uncomfortable allowing a trustee to do this. Similarly, the trust should discuss whether the successor trustee should have the ability to trade trust assets on margin. Many times revocable trusts are set up so that the successor trustee will have the same powers as the original trustee. However, it does not have to be this way. A settlor may not want a successor trustee to have the same powers as the settlor did as trustee. This usually means limiting the successor trustee to investment strategies that are not risky.

Minors Clause

Most people love their children and want them taken care of when they pass away. Similarly, people love their grandchildren and want them provided for. What people do not want is for their child to get a windfall of cash upon their death and to spend it all on frivolous things. Young people are prone to act irresponsibly. So, when an individual is creating his or her revocable trust it is strongly suggested that the trust include a provision for minors.

A minors clause is a provision that makes all assets to be distributed to individuals under the age of 18 to be held in trust. This prevents a beneficiary who is a minor from receiving a large sum of cash and spending it. The money would be held in trust with a trustee who would manage the money and distribute it for the benefit of the child.

Many of these provisions include other language that holds the money in trust until the beneficiary is as old as 35. Some people are less responsible than others so trusts can have provisions to account for the circumstances of each beneficiary. The great thing about the revocable trust is that it is flexible enough to account for special circumstances and individual needs.

Simultaneous Death Clause

A revocable trust should provide for the possibility of a settlor and spouse dying in a common disaster. Most individuals set up their trusts to pay out to their spouse upon their death. The spouse's trust has an identical provision and both trusts direct the assets to be distributed to their children upon both of their deaths. If the trust does not have a provision that presupposes the death of one of the spouses before the other, in the event of a common disaster, there could be great problems in the administration of the trusts. The successor trustees would have to agree on which trust would distribute assets to the beneficiaries. If the spouse's trusts did not have the same beneficiaries upon the death of both settlors, there would be enormous problems in the administration of the estates. Lawsuits would follow and the attorney's fees would be very high.

It is suggested that a revocable trust should contain a provision that provides, in the event that the settlor and his spouse die in a common disaster, it shall be assumed that the husband predeceased the wife. This is just for simplicities sake, the trust could just as well provide that it shall be assumed that wife predeceased the husband. Either way, a simultaneous death clause should be included when the settlor has a spouse.

Incapacity Provision

A revocable trust can be set up to avoid a guardianship in the event of the incapacity of the settlor. An incapacity provision should be included in a revocable trust. The incapacity directs that in the event of the incapacity of the settlor, the successor trustee shall take over the duties as trustee of the trust.

The incapacity provision should state that the incapacity of the settlor should be determined by two physicians who have examined the settlor and find the settlor can not manage his own affairs. An incapacity provision should also state the settlor's intent to stay in his home as long as possible, unless the settlor wishes to go into a long term care facility. Most people, however, would like to remain in their home in the event of their incapacity.

This provision is essential to prevent a court ordered guardianship in the event of incapacity. A guardianship is expensive and time consuming for the individual acting as guardian. To not include the incapacity provision would be to ignore one of the greatest tools a revocable trust can provide.

Revocability

It seems obvious, but a revocable trust should include a provision that states that the trust is revocable. That provision allows for the trust to be revoked. The revocability provision should also state that the settlor may amend the trust and alter it in any way he chooses. These are key provisions in a revocable trust. If the trust does not state that the trust can be revoked, altered, and amended, the trust does not afford many of the benefits it should.

The only reason to not include a revocability clause would be to make the trust an irrevocable trust, which will provide protection from creditors if the trustee is someone other than the settlor. The trust would then also serve as a good way of gifting away assets during your lifetime and taking advantage of the unified tax credit. This trust would then be a completely different trust than a revocable trust with different advantages and disadvantages. If someone wishes to simply avoid a probate proceeding upon their death with control of their assets during their lifetime, the trust should include a revocability clause.

There may be some circumstances where a settlor would not want a trust to be revocable or amendable. As an example:

Mr. Smith is a widower with sizable assets. He has two daughters named Mary and Jane. Mary is a good girl and is very responsible. Jane is completely irresponsible and has an affinity for the finer things in life. Jane is constantly pressuring her father for money and threatening to keep Mr. Smith's only grandchild, Jimmy, from him unless he helps Jane buy a new Mercedes. Mr. Smith gave into Jane on many occasions and when the market started to drop he lost a great deal of money. If he had not given so much money to Jane he could have invested in bonds, which are less risky than stock, and he would be fine financially. Mr. Smith now has to sell his home on the beach in Florida and move into a condo inland.

Assume for a moment that instead of just giving in to Jane's demands, Mr. Smith goes to see an estate planning attorney. Mr. Smith tells his story of woe to the attorney and he tells Mr. Smith that there is a solution. The lawyer tells Mr. Smith that he can transfer all of his money to an irrevocable trust for his benefit. He can name his daughter, Mary, as trustee because she is responsible and always does the right thing. With Mary acting as trustee, Jane will have to beg her sister and not her father for that money. As trustee, Mary will have a fiduciary obligation and will have to deny any request by Jane. Mr. Smith will still get to see Jimmy and his money will be safe from his greedy daughter Jane.

AB Trust

An AB trust is actually not a trust, it is two separate revocable trusts set up for a married couple. The AB trust is used to maximize the unified tax credit. The unified tax credit is a tax law that states than an individual can gift during his lifetime or at death a specified amount. That amount is currently $1.5 million. The amount will be going up over the next few years as shown in the following chart.

Year	Unified Credit/ Exclusion Equivalent
2002 - 2003	$1 million
2004 - 2005	$1.5 million
2006 - 2008	$2 million
2009	$3.5 million
2010 and beyond	No Estate Tax

The AB trust maximizes a married couple's unified tax credit by creating a residuary trust upon the death of the first spouse. The trust of the first spouse to die directs that the residuary trust be funded with the maximum amount allowed to be passed free of tax and be allocated to the residuary trust held for the benefit of the surviving spouse. This means that the first spouse uses the $1.5 million dollar unified tax credit. This prevents the money from going to the surviving spouse's taxable estate. Since the money is in the residuary trust, when the surviving spouse passes away another million dollars can be passed along to beneficiaries free of estate tax. The residuary trust will pay out income to the surviving spouse during his or her lifetime and upon his or her death, the trust will pay out to the beneficiaries designated by the original settlor. The money left over after the $1.5 million is used to fund the residuary trust can pass either directly to the surviving spouse or another trust can be created. Often, especially with second marriages, the money in excess of $1.5 million is held a trust so the children of the first spouse to die cannot be disinherited.

Illustrations

Edna and Ira Klein have assets worth approximately $2 million. They have set up AB trusts for the benefit of one another and, upon the death of both, their assets are to pass to their son Jeremy. Edna passes away. Since $1.5 million in assets were titled in the name of Edna's trust and $1.5 million dollars in assets were titled in the name of Ira's trust, no estate taxes are due. Edna's assets pass to a residuary trust for the benefit of Ira during his lifetime. Unfortunately, Ira dies a week after Edna. Edna's residuary trust now will be distributed to Jeremy. Ira's trust will be distributed to Jeremy. No taxes will be due because $1.5 million passed through Edna's estate and $1.5 million passed through Ira's estate.

Assume now that Edna and Ira did not have AB trusts. They both simply had trusts that paid to each other, free of trust, upon each of their death and then to Jeremy upon the death of the survivor. When Edna dies, all of her assets pass to Ira. Since Edna only had $1.5 million in assets, no estate is due . Ira now has $2 million in his trust, so when Ira dies, his estate will have to pay estate taxes because Ira's estate is over the $1.5 million mark.

Execution Clause, Similar to a Will

The execution of a revocable trust should be the same as the execution of a will. The execution of a will needs to be done with some degree of formality. In most states, a will needs to be signed in front of two disinterested witnesses and a notary. All of the parties need to be present at the time of execution for the will to be valid. A revocable trust should be executed with the same formality to insure its validity. Since a revocable trust is prepared by an attorney, the trust document should be executed in the attorney's office in front of two witnesses and notarized. This makes it easier to make copies for the attorneys records and easier for the client, who will not have to hire a notary.

Chapter 8
Funding a Trust

Importance of Funding

A revocable trust does not help avoid probate if the trust is not funded with assets. A trust is funded by re-titling assets from an individual's sole name and into the name of the trust. The title of the trust is the name of the trustee along with the name and date of the trust. The funding process usually involves contacting financial institutions and informing them that you wish to re-title your account with them. The financial institutions have their own forms that they require to be filled out. This is a minor hassle, but it must be done in order to fund the trust. Remember, if the trust is not funded it has no assets and it does nothing to avoid probate.

Assets placed in a revocable trust do not lose any of the characteristics they had when they were owned in the settlor's individual name. There is no drawback to funding the trust except the time that needs to be expended doing it.

What to Put in the Trust

All sole name assets that would be subject to probate if an individual were to die should be placed in the revocable trust. Avoiding probate is the main purpose of the trust. Assets that should be placed in the trust include:

- Bank accounts
- Brokerage accounts
- Real property
- Business interests
- Partnership interests
- Stocks, bonds, CDs, treasury notes, etc.

Some assets may not need to be placed in the revocable trust. For example, insurance policies may not need to be titled in the name of the trust if the beneficiary designations are done properly. The proceeds from the policy will not be probated if a beneficiary is listed. Other assets such as IRAs should not need to be titled in the name of the trust if beneficiaries are properly designated. IRAs have special tax rules associated with them which may make it unwise for the IRA to be placed in the revocable trust.

Personal Property

Most states have laws that exempt personal property from probate. This means that it is not necessary to title personal items in the name of a revocable trust. Certain personal items may have considerable monetary value. These items should be titled in the name of the trust because they may be included in the estate for federal or state estate tax purposes.

In order to transfer personal property into a trust, an individual simply needs to assign his interest to the trust. This is done by signing a document describing the property to be transferred that states that you are transferring it to the revocable trust you have created.

An automobile may need to be titled in the name of the revocable trust to avoid probate. Some states require that an automobile go through probate upon the death of the owner, regardless of the value of the car. It is important to know the rules of the state in which you reside to plan correctly. Regardless of what state you are in, if you own a valuable car or a collectable car it should be placed in your revocable trust so that it does not have to go through probate.

Business Interests

Business interests are subject to probate if they are owned in an individual’s sole name at the time of death. As such, business interests should be placed in an individual’s revocable trust to avoid probate.

Business interests, such as stock ownership, should be placed in an individual’s revocable trust. In order to transfer the title of stock, the interest needs to be assigned to the trust. Stocks can be re-titled by contacting the brokerage house they were purchased through and having them re-title the interest.

Certain business interests are virtually worthless if owned by someone other than the decedent. Business interests associated with sales, service-based businesses, and business interests based on the highly specialized skills of the decedent are worth very little upon death. If the business does not own any assets it is virtually worthless because it was only the owner’s good will and specialized skills that were marketable. These types of business interests can be placed in a revocable trust by assigning the interest.

It should be mentioned that some states do not allow certain business interests to be owned by a trust. Subchapter “S” stock cannot be held by a trust unless specific language is placed in the trust.

Assets with Beneficiaries

Assets with designated beneficiaries do not need to be titled in the name of a revocable trust. The assets will pass outside of probate to the beneficiaries as long as the designation is proper. However, most people should transfer those assets to the trust because the trust will provide for all the assets and has provisions in case one of the beneficiaries passes away before the settlor.

It is a good idea to name the trust as the primary beneficiary of an asset. A revocable trust already designates how a person wishes all of his or her assets to be distributed upon his or her death. By passing assets by other means, assets are not going to be distributed according to the terms of the trust. This could lead to an unwanted result. Children could end up upset, with feelings of rejection, because a parent left more assets to another child. The worst result would be that the asset outside of the trust is the only asset remaining at the time of an individual’s death. It would be the only asset and it would not be divided according to the trust, but given all to a designated beneficiary.

How to Transfer Assets

As discussed, different assets are transferred into the revocable trust by different means. Real property is conveyed by deed from the sole name of an individual to his or her revocable trust and recorded in the county where the property lies. Stock is re-titled by filling out a change of ownership form. Personal property is transferred to the trust by assigning one's interest to the revocable trust. Some of the transferring must be done with the aid of an attorney, but most of it is done by contacting the institution where the asset is held and filling out a form. Regardless, the aid of an attorney can be helpful.

Letter to Broker

Once a revocable trust has been created by an individual, a letter should be sent out to all of the institutions where the individual has sole name assets. The letter should state that the individual has created a revocable trust for the purpose of avoiding probate. The letter should include the account number, a description of the assets, and the proper name of the trust in which they are to be re-titled. This letter is usually sufficient but, if not, it is usually a good way to find out what more needs to be done to re-title the assets. Some institutions require a copy of the trust document while others need a specific form filled out. Either way, the broker letter is a good way to start the re-titling process.

Banks

Accounts held in an individual's sole name at a bank should be re-titled into the name of his or her revocable trust. The bank should be notified, by means of a broker letter, that the account holder intends to re-title his account into the name of his revocable trust to avoid probate upon his death. The bank will usually request a copy of the trust for its legal department to review. There is no need to be concerned about privacy issues because the bank is not allowed to disclose the information in the trust. The trust just provides the bank with the information necessary to administer the trust according to the provisions. Banks frequently have additional forms and signature cards that need to be filled out as part of the re-titling process. The work involved in the re-titling of a bank account is usually minuscule in comparison to the work that would need to be done regarding the account if it were left in the individual's sole name and thus subject to probate.

Schedule A

Schedule A of a trust is an addendum to the trust that lists all of the assets in the trust. This list is not always complete or even in existence. It does not matter if Schedule A is complete. Schedule A is just an aid to the successor trustee to track down assets in the trust. Just because an assets is not listed on Schedule A does not mean that the asset is not titled in the name of the trust. The legal title of an asset is the determining factor regarding whether an asset is in the revocable trust or not.

It is wise to list all assets in the trust on Schedule A of the trust. It makes it much easier for the successor trustee to track down assets and administer the estate. Additionally, it provides a convenient reference sheet for the current trustee to plan his estate.

Warranty Deeds and Quit Claim Deeds

Real property should be held in the name of an individual's revocable trust because if it is owned as a sole name asset it is subject to probate. Property can be conveyed by several types of deeds. One type of deed is a quit claim deed. A quit claim deed is a conveyance of property by which the owner simply transfers ownership of a piece of property. A quit claim deed makes no warranties and does nothing but transfer legal title of the property to another individual.

A warranty deed is a conveyance of property whereby the ownership of a piece of property is conveyed to another individual, while warranting that the owner has good marketable title. The warranty deed usually warrants the marketability of a piece of property and gives the new owner extra insurance about the property being deeded.

Many title insurance companies insist that property deeded to a trust be done so by warranty deed. There should be no reservation by the settlor for doing so since the property being conveyed will still be owned by the settlor. The settlor will essentially be making warranties to himself. It is common, however, for property to be deeded to a trust by means of a quit claim deed. Either way, the trust attorney can prepare and record such deeds without much, if any, difficulty.

Mortgaged Property

Mortgaged property can be placed in a revocable trust. As a matter of fact, most people mortgage their homes. The problem with placing mortgaged property in a trust is that most mortgages contain an acceleration clause. An acceleration clause states that a mortgage becomes due once it is transferred. Technically, a transfer to a revocable trust would cause the acceleration clause to kick in. Most, if not all, mortgage companies do not enforce the acceleration clause. It is important to check with your mortgage company before you place mortgaged property into your revocable trust.

Mortgaged property is placed in a revocable trust just like any other property. The property is deeded into the name of the settlor, as trustee, of the revocable trust. The property will then be owned by the trust, while the settlor retains all of the benefits of ownership.

Homestead Exemption

Some states provide for creditor protection for specific kinds of property. For example, in Florida, the property must be an individual’s primary residence and be resided in over six months out of the year. If a piece of property meets these qualifications, the property cannot be attached by creditors. The property will also qualify for a property tax exemption. If the property is placed in a revocable trust, the settlor will not lose the homestead exemption. The settlor will not lose the homestead because he will still retain a significant enough interest in the property, as trustee and beneficiary. It is important that the settlor re-apply for the homestead exemption with the newly titled property. If the settlor does not re-apply for the homestead it could be lost for up to a year or until the settlor re-applies.

Tax Implications of Transferring to Trust

There are no tax implications for placing your assets in your revocable trust. The revocable trust does not need to file a separate tax return and the settlor’s Social Security number is used as the trust’s tax ID number. Assets in the trust are not taxed at different rates than assets held in an individual’s sole name and there are no gift tax implications for transferring assets to a revocable trust.

Chapter 9
Administration of Trust During Lifetime

No Separate Tax Returns

A person does not have to file a separate tax return for the assets placed in a revocable trust. The assets in a revocable trust are treated as though they are owned by the settlor for federal and state income taxes. The rate at which assets in a revocable trust are taxed is the same as the rate which assets owned in an individual's sole name are taxed.

There are simply no tax ramifications for placing assets in a revocable trust. As a matter of fact, Congress passed a law in 1981 that stated that a Form 1041 (Trust Tax Return) does not need to be filed for a revocable trust. Once a trust becomes irrevocable, like upon the death of a spouse, a Form 1041 needs to be filed every year. That tax return is separate from an individual's tax return and should only contain information pertaining to the irrevocable trust and not the individual's sole name assets or separate revocable trust.

Amendments

A revocable trust may be amended, occasionally, by the settlor. Upon the death of the settlor, a trust usually becomes irrevocable and the successor trustee is unable to amend or alter the trust. However, while the trust is revocable and the settlor is alive, a settlor can alter the trust through a mechanism called an amendment.

An amendment should specifically and clearly reference the original trust and the date it was created. It should also reference the provision in the original document that explicitly states that the trust can be amended. In this way, there will be no questions as to the veracity of the trust amendment. A trust amendment should also be executed with the same formality and requirements of the original trust document.

An amendment to a trust can alter any substantive provision of the trust. In fact, the amendment can even make the trust irrevocable or unable to be amended. Most trust amendments center around gift provisions and provisions regarding successor trustees. People who create trusts often wish to alter the amount of gifts given to children and grandchildren due to changed circumstances. An amendment to a trust allows a settlor to account for changed circumstances or a change of mind. As for provisions regarding successor trustees, it is often necessary to name a new successor trustee because of a death or a change in life circumstance.

Amendments can be done for any number of reasons and to any number of elements of a revocable trust. It is not the job of a lawyer or financial advisor to comment on changes in gifts made by the trust. But, it is the job of a lawyer or financial advisor to advise on the possible consequences and wisdom of certain changes to trust documents. For instance, it may not be the best decision for a settlor to amend his trust to name eight people a successor trustee instead of one. This would make the administration of the estate difficult. Additionally, it may not be wise for a settlor to amend his or her trust to gift his or her entire estate to 50 different charities because of the problems involved in the accounting and administration. The settlor should be advised to select a few beneficiaries to receive a larger share each. In these ways, an estate planner can guide an individual to make wiser decisions and not make decisions for them.

Some people will abuse their ability to amend a trust. These people use their ability to alter the terms of the trust as a threat of disinheriting their children. While this is often an effective tool in altering children's behavior, it is also time consuming, confusing, and annoying to the practitioner preparing the amendments. Clients should be advised to think long and hard about the provisions of their trust and not get in the practice of altering their revocable trust every time they get into an argument with their children. In many instances people have altered their trust so many times that they are not quite sure what it says. This is bad practice and should be avoided.

Chapter 10
Other Advantages of a Living Trust

Avoids Guardianship

Much like the way a revocable trust can be used to avoid probate, a revocable trust also can be used to avoid guardianship. Guardianship is the judicial supervision of a guardian taking care of an incompetent individual and his or her assets. When a person loses the ability to manage his or her own affairs, the government will step in and protect his or her interests. The government does this by holding a court proceeding where the court listens to the testimony of experts and witnesses. This hearing determines whether the individual is competent to manage his or her own affairs. If the court determines the individual is unable to manage his or her own affairs, the court will appoint a guardian. The guardian’s job is to mange the individual’s affairs and report back to the court. The guardian must file an accounting every year and keep the court informed of every dollar spent. The guardianship is expensive and time consuming.

If the incompetent person has all of his or her assets in a revocable trust, a guardianship proceeding is not necessary. The revocable trust has an incapacity provision. The incapacity provision states that upon the incapacity of the settlor, the successor trustee shall take over the duties of the trustee and manage the trust for the benefit of the settlor. The incapacity of the settlor is determined by letters from two attending physicians of the settlor. The doctor’s letters need to state that the settlor is incapable of managing his or her own affairs.

The revocable trust prevents the need for the guardianship proceeding. The cost of replacing the trustee with the successor trustee is the cost of the successor trustee’s fee. That fee is usually about 1 percent to 2 percent of the value of the trust annually and most of the time it is a loved one who will not charge. Either way, this cost is significantly less expensive than the cost of a guardianship. The administration of a revocable trust does not require an attorney.

How Does It Work?

As described above, when the settlor of a revocable trust loses the ability to manage his own affairs, the successor trustee of the trust can be appointed to act as trustee of the trust. The incapacity provision of the trust states that upon the incapacity of the settlor, who is acting as trustee, the successor trustee is to be appointed to act as trustee. The incapacity of the settlor is determined by the attending physicians of the settlor. The settlor’s doctors need to prepare letters stating that the settlor is incapable of handling his own affairs. Those doctor’s letters, along with a copy of the incapacity provision of the trust are enough to appoint the successor trustee as trustee. The successor trustee can then carry out the terms of the trust for the benefit of the settlor as if he or she were the original trustee.

Successor Trustee

The successor trustee is named in the original trust document. The successor trustee is the person named to take over the duties as trustee of the revocable trust upon the death or incapacity of the settlor. The successor trustee's duties will vary if the settlor is incompetent or deceased. If the settlor is incompetent, the successor trustee will usually be carrying out the terms of the trust for the benefit of the settlor. That would involve paying the settlor's bills, investing for the settlor, and managing the settlor's accounts. If the settlor is dead, the successor trustee will usually administer the trust according to the distribution provision.

Privacy

A revocable trust is a private document. It does not need to be recorded to be effective. Since the trust is not recorded, the trust is not a matter of public record. While some financial institutions may request a copy of the trust, the institution's purpose is not to find substantive information but to determine the binding provisions of the trust. Financial institutions are interested in the legal ramification of a trust, such as what powers the trustee has. They are not interested in knowing or disseminating the information contained in a trust. Financial institutions are not allowed to convey the information in the trust to unauthorized individuals.

When an individual with sole name assets passes away, the estate needs to go to probate. A probate proceeding is a matter of public record. The public nature of a probate proceeding invites creditors and individuals to make claims against the estate. It also allows private information to go public. That is unnecessary. No one needs to know the value of another individual's assets.

Will is Public Record

A will is a legal document that describes what an individual would like to have happen to his or her assets upon his or her death. A will keeps an individual's assets from being subject to a state's intestacy statute. An intestacy statute describes how an individual's assets are to be distributed in the event he or she dies without a will. A will does not avoid probate. A probate proceeding is a matter of public record. All of the information disclosed in a probate proceeding is a matter of public record.

Trust is Not Public Record

Assets in a revocable trust at the time of the settlor's death are not subject to probate. The assets in the revocable trust are distributed according to the terms of the trust. A trust document is not a public document, it is private. The information contained in the document is only disclosed to the trustee and the beneficiaries of the trust. The beneficiaries are only entitled to the specific accounting information and have no right to information regarding other beneficiaries or even who they are. A trust is a private document and the information contained in it is private as well.

Smoother Transition of Assets

When an individual passes away, his or her assets need to be distributed. The assets should be distributed according to the person's wishes. If the individual did not leave a will, or a trust, and has assets that do not have designated beneficiaries, the individual's assets will be distributed according to the state's intestacy statute. The intestacy statute usually states that assets are to be distributed to the surviving spouse, if one exists or is alive, otherwise to the children. The distribution of assets is slow because the estate needs to go through probate and then is distributed according to the intestacy statute. This results in the slowest distribution of assets possible.

If an individual passes away with a will and sole name assets, the estate must go to probate. The court will oversee the distribution of assets according to the terms of the will. The distribution of assets will take up to two years depending on the amount of assets and legal battles that may occur.

If an individual passes away with no sole name assets and all assets titled in the name of the revocable trust, the distribution of assets will go smoothly. All that is required is to have the successor trustee appointed and change the title of all of the trust assets. The assets will be re-titled to the successor trustee's name as trustee of the trust. The assets can then be distributed according to the terms of the trust. The distribution could be stalled by federal and state estate tax liability depending on the size of the estate. The successor trustee cannot distribute all assets until the tax liability has been determined because the successor trustee cannot calculate the specific amounts due to beneficiaries.

Harder to Contest

The private nature of a revocable trust makes it harder to contest than a will. Because anyone can read your will once you have passed away, the information is readily available. All an individual needs to do is go to the county courthouse and request the information. That information may provoke a lawsuit or a will contest. Will contests are especially ugly because they involve family members fighting over money.

With a revocable trust, only beneficiaries are entitled to information. People have no idea what assets you left behind and how they are being distributed. The successor trustee will provide beneficiaries with notice and give them an accounting of what assets are in the trust. The beneficiaries are also entitled to a copy of the trust. If they do not share this information, no one other than the attorneys and accountants handling the estate administration will have any information on the estate. Attorneys and accountants are not allowed to disclose that information because it is confidential.

Undue Influence

One way to contest a will or revocable trust is to claim that someone exerted undue influence or forced the person to do what they wanted rather than the wishes of the settlor in the creation of the will or trust. If it is proved in court that someone exerted undue influence over an individual in the creation of his or her will or revocable trust the document will be found invalid.

Depending on the rules of the state that you are in, the result of a will or trust being declared invalid could vary. It could result in the estate being treated as though the deceased individual passed away intestate, without a will. If an individual passes away intestate, his or her estate will be subject to the states intestacy statute. The rule could also be that the court would find that the previous will or trust, that was not created under undue influence, created by the individual will be binding. This means that the will or trust created by the individual and which he or she attempted to revoke will be the one that governs. Neither of these results are the intent of deceased individual.

It is harder to make an undue influence claim against a trust than a will because it is harder to get information regarding a trust. The information regarding the will is public record. So, the individual seeking to claim undue influence will have a harder time ascertaining information regarding a trust than a will. Another reason it is harder to make an undue influence claim under a trust than under a will is because the settlor of a trust acts as trustee. The settlor's role as trustee means that he had to take an active role in the administration of the trust while alive. An individual would seem to be less apt to be influenced to gift away assets if he is actively re-titling those assets and managing them.

Lack of Testamentary Capacity

A trust can be challenged on the grounds that the settlor lacked the capacity to create the trust and understand its ramifications. This also is a difficult claim to make with a trust. A trust is a complex document that requires an attorney eliciting a great deal of information from the settlor. It would be difficult for an incompetent individual to convey all of that information to an attorney. A trust also requires the settlor, as trustee, to re-title assets into the name of the trust. This is not the toughest job in the world but it would be almost impossible for an incompetent individual to fund a trust.

A claim that an individual lacked capacity to create a will is easier to make than a claim against a trust. A will is a document that is created and usually forgotten about until its creator becomes ill or passes away. The information that needs to be conveyed to the attorney creating it is minimal. An attorney may never realize that the individual creating the will lacks testamentary capacity. The meeting between the attorney and client may only last 20 minutes, not giving the attorney cause for concern.

Chapter 11
Ancillary Documents

Pour-Over Will

A pour-over will is a safety precaution that should be used when creating a revocable trust. A pour-over will states that upon the death of the testator all assets titled in the testator's sole name should be distributed to the testator's revocable trust and distributed according to its terms. The assets that pass through the pour-over will still need to go through probate because they were titled in the sole name of the decedent. The pour-over will makes the administration of the estate much easier because the assets will all be placed in the trust, albeit through the probate process. The trustee can then distribute the assets according to the terms of the trust, which was the settlor's intent all along.

Provisions regarding the custody and guardianship of minor children need to be placed in a will and not in a trust. The pour-over will is the perfect way to express who a person wishes to look after his or her children upon his or her death. The pour-over will can state the intentions of the testator, or creator of the will, regarding the custody of his or her minor children and provide a safeguard in case the trust was not funded completely.

How to Distribute Personal Belongings

Most personal belongings are not highly valued. In most states, personal belongings do not go through probate. The court allows personal belongings to be passed along outside of probate because it is not worth the court's time to deal with it. In these states, personal belongings usually do not need to be titled into the name of a revocable trust since they pass outside of probate. To be on the safe side, however, they can be placed in the trust by means of an assignment. The assignment should describe the personal belonging and title in the name of the revocable trust. It is necessary to assign highly valued personal belongings to the trust so they do not need to be probated.

Personal belongings passing outside of probate can be devised in the pour-over will. People usually just distribute them to the surviving spouse, and if none, in equal shares among the children. This may not be advisable if you believe that your children will have a hard time dividing your personal belongings. Often, children fight over small and inexpensive things. One of those things may be your personal belongings to which they have placed some emotional or sentimental value. As such, it may be advisable to specifically mention what belongings you wish to go to whom. This may be time consuming but it could prevent a fight after you pass away. In most states, an individual can make a list of his or her personal items and direct to whom they wish them to pass.

Tangible Personal Property List

A tangible personal property list is a list of personal belongings designating whom an individual wishes them to pass to upon their death. The list is attached as a schedule to the last will and testament. The list, in most cases, can be created after the creation of the will. All the testator needs to do to make the list effective is to sign it. It does not require the formalities of execution like a will.

The list is a great tool for distributing personal items. Items can be accounted for even if they are acquired after the creation of the will. The list also allows the testator to change his or her mind about who is to receive the belongings. These changes can be done without the supervision of an attorney.

The tangible personal property list should be kept with the will so upon the testator's death the list will be found and the decedent's wishes will be granted. The list is not all inclusive, meaning that assets not on the list do not go to the state or to charity. If a personal belonging is not mentioned on the list then it is simply divided according to the terms of the will, or the trust if it was assigned to the trust.

Who to Name as Executor or Alternate

The person named as the executor of a pour-over will should normally be the same person named as the successor trustee under the terms of the revocable trust. If the successor trustee and the executor are the same person the administration of the estate will go much more smoothly. The successor trustee will simply be re-titling assets into the name of the trust and distributing according to the terms of the trust. Since the will has the pour-over provision, all of the assets will go through the trust.

People normally name surviving spouses as successor trustee and executor because they normally leave all of their assets to them. This means that they are only accountable to themselves. This is much easier than when numerous beneficiaries are receiving money. When there is no surviving spouse, people normally choose their oldest or most responsible child to act as the executor.

The other consideration that needs to be made in determining an executor is whether the individual chosen to act is a resident of the state in which the testator resides. Most states require that an out of state executor post a bond. The bond assures the court that the executor will not try to run off with the assets or mismanage them. It is a form of security. So, in most cases, it is recommended to choose an executor who is a resident of the same state so bond is not required. Some states do not allow out of state individuals who are not family members to be the executor. A minor cannot act as an executor.

It is important to name an alternate to the named executor in case the named executor is unable or unwilling to act. If no one is named, the court will appoint someone to act. To prevent this it is wise to name an alternate. As an alternate to the named executor, many people choose someone who is significantly younger than the named executor. This is done to assure that the alternate is alive or healthy at the time of his or her death. This person is usually one of his or her children. If someone does not have children then he or she can choose a friend or an attorney.

Durable Power of Attorney

A durable power of attorney is a legal document that appoints an individual as an agent to act on behalf of another individual. The person appointed as power of attorney has the power to act immediately. The power of attorney is not valid for assets owned by the individual's revocable trust. It is important to understand that the durable power of attorney is only good for sole name assets. A durable power of attorney can be written to be broad and include the power to do anything the named person wishes or it can give only limited powers. The power of attorney is most useful when the agent is given broad powers.

A durable power of attorney is a useful tool when an individual has sole name assets and is becoming incompetent. The power of attorney can manage the sole name assets of the incompetent individual or re-title them into the name of the revocable trust and can be used to avoid guardianship. The power of attorney acts as a safeguard in case assets are accidentally not placed in the trust. However, the durable power of attorney terminates upon the death of the creator.

The person who is named as the power of attorney should be selected carefully. The person who is given power of attorney can control all of an individual's sole name assets, so it is important to appoint someone you trust. Most people appoint a spouse or the oldest or most reliable child. If someone does not have family, he or she should choose someone he or she trusts. The person named as power of attorney should be the individual named as successor trustee and executor of his or her estate. This will make the transition easier when the person passes away. A power of attorney can be revoked.

Springing Power of Attorney

A springing power of attorney is a legal document that appoints an individual to act as an agent for another upon the incapacity of the appointing individual. The springing power of attorney has the same characteristics as a durable power of attorney except that it is not effective upon execution, but upon the incapacity of the person who creates it.

Effective when Signed

A durable power of attorney is effective when signed. A springing power of attorney is effective upon the happening of a specific event, namely the incapacity of the creator. Neither the durable power of attorney nor the springing power of attorney is effective upon the death of the person giving the power of attorney.

Who to Name?

The person appointed as an agent in the durable power of attorney has the power to write checks from an individual's accounts, sell stocks in an individual's name, and even liquidate accounts. Essentially, the durable power of attorney gives the agent control over all of an individual's sole name assets. The decision on whom to appoint as the agent is important.

The simplest way to choose the agent for the durable power of attorney is to choose the person appointed as the successor trustee under the terms of the revocable trust. This is not always practical because the successor trustee may be out of state. It is difficult for an agent under a durable power of attorney to act from out of state. The agent normally only acts when the individual is unable to do so. The agent helps out in day-to-day activities, which is difficult if not impossible to do if out of state. So, the agent should be a trusted person who lives close to the individual. Most people choose their spouse or oldest child to act as their agent. A close friend is an acceptable substitute if an individual has no immediate or close family.

Health Care Surrogate

All states allow an individual to designate an agent to make medical decisions on his behalf. This should be done by every individual, regardless of age, to insure that someone he trusts can make medical decisions for him in the event of an emergency and in the event he is incapable of making decisions himself.

A health care surrogate is appointed through a designation of health care surrogate or a medical power of attorney. The medical power of attorney is unlike the durable power of attorney in two regards.

- A medical power of attorney appoints an agent to make medical decisions for an individual if he is unable to do so for himself. A medical power of attorney does not give the agent the authority to deal with the individual's financial affairs.
- It is only effective when the individual cannot make decisions for himself.

Who to Name?

The designation of a health care surrogate is an important decision. The decision is potentially a life or death decision. The health care surrogate has the authority to authorize surgery, initiate treatment, and refuse treatment. This said, the person chosen to act as the health care surrogate should be a person one trusts implicitly. That is why most people choose their spouse to act as their health care surrogate. When the individual does not have a spouse, he or she usually chooses one, or all, of his or her children. If the individual does not have immediate family, a friend should always be chosen over a corporate agent.

Unlike choosing a successor trustee, a corporate fiduciary should not be an option in appointing either a medical power of attorney or durable power of attorney. Corporate fiduciaries are undesirable as agents for numerous reasons. Corporate fiduciaries usually do not accept the responsibility and, if they do, they are generally unresponsive. Corporations are large and it is just too hard to trust important personal decisions to them.

Living Will

A living will is a legal document which states that an individual does not want to be kept alive artificially and allows an individual to die with dignity. The document also states that artificial means are not to be used in the case of a permanent vegetative state or a terminal end stage condition. In short, the living will is only used when there is no chance that an individual can be rehabilitated from a vegetative state.

Not all people wish to have a living will, for personal or religious reasons. It is simply a tool that can be used for an individual to inform the doctors of their wishes. The document also makes it easier on the health care surrogate who will not be forced to make the decision to terminate a loved one's life. It is traumatic for a loved one to decide to terminate life support or artificial life support, even when there is no chance for rehabilitation. That decision should be made by an individual while competent, long before the situation arises. This will make the sadness of an individual's passing less traumatic for the family.

Different from a DNR

A do not resuscitate (DNR) order is an instruction given by an individual to his or her physician to not give him or her any medical attention in the case of serious trauma. The do not resuscitate order is very different from a living will which is a document prepared by an attorney to express the individual's desire to not be kept alive in a vegetative state by extraordinary means. The difference is that a living will is not a refusal of medical care, just a refusal of extraordinary care when recovery is impossible.

Chapter 12
Other Ways to Avoid Probate

Joint Tenancy

Joint tenancy is any type of ownership that involves more than one individual owning an interest in property. Joint tenants have different rights than tenants in common and tenants by the entirety. Each joint tenant owns an undivided interest in the property. The undivided interest means that both tenants own the entire piece of property and have a right to the entire property as long as they own their interest. Most states assume that joint tenants have survivorship rights, meaning that the property automatically passes to the surviving tenant, but there are states that do not assume survivorship rights and upon the death of a joint tenant the interest of the other is an asset of the estate to be passed on to heirs. This is because certain states refer to joint tenants in common as joint tenants. The confusion caused by the nomenclature can cause problems.

Joint tenancy can be used as a tool to avoid a probate proceeding. The death of one tenant will result in either the interest passing to the other tenant by operation of law or passing to the heirs of the decedent through a probate proceeding. It is important when titling property owned with another individual to be sure how the property will be distributed upon the demise of one of the tenants.

With Right of Survivorship

The addition of the words, “with right of survivorship,” is one way to assure that upon the death of one of the tenants the property will not need to be probated. The property will pass by operation of law to the other tenant outside of probate. This is the most common way married couples own their assets and can be an effective tool used by estate planners to avoid probate, but it can have several disadvantages.

First, a joint tenancy with rights of survivorship does not prevent probate if both of the joint tenants die at the same time. If the joint tenants die at the same time, the court must determine which one died first and then that individual’s estate must open a probate proceeding with the court to distribute the asset. The possibility of two individual joint tenants dying at the same time is not all that inconceivable. People frequently die in common disasters such as car accidents and natural disasters. An estate plan should account for this possibility.

Even if the joint tenants do not die at the same time, the joint tenancy may not avoid a probate. People often die within a short time after their spouse’s death. If the asset is not re-titled before the second joint tenant’s death, the asset must be probated. A spouse passes away and the survivor does not have time nor the inclination to worry about re-titling assets to avoid probate. The survivor is then subjecting the family to the problems of probate.

The only fail-proof way to avoid probate is a revocable living trust. The trust accounts for the possibility of a common disaster and the survivor, if one passes away, may have very little to deal with to protect their estate.

Definition and How it Works to Avoid Probate

Joint tenants by definition own an undivided interest in jointly held property. The joint tenant's interest is not in half of the property, but the entire property. Each joint tenant "owns" the entire property.

Joint tenancy works to avoid probate because upon the death of one of the joint tenants the other tenant owns the property automatically. The surviving tenant needs nothing more than a death certificate to re-title the property into their individual name.

Advantages

The advantages to titling property as a joint tenant with another over creating a revocable trust are that it is cheaper, easier, and involves less work. It does not cost anything to re-title property such as bank accounts or brokerage accounts as joint tenants. Creating a revocable trust can cost between $200 and $3,000. Re-titling real property as joint tenants can cost up to $100 for attorney's fees and recording fees, but that same cost will exist if a revocable trust is created. The property will need to be deeded to the trust.

Creating a revocable trust involves a great deal of thought and planning. Deciding how to distribute assets, meeting with an attorney, and planning takes a significant amount of time. Changing account titles from an individual's sole name into the name of the individual's name with a joint tenant is much easier. It is also a lot less work. When a revocable trust is created, banks and brokerage houses often require additional paper work be done and copies of the trust be provided.

Avoid Probate

Property owned as joint tenants avoids probate as long as the survivor has survivorship rights and is alive at the time of the other tenant's demise. Joint tenancy works to avoid probate because upon the death of one of the joint tenants the other tenant owns the property. The property passes to the surviving tenant by operation of law. The surviving tenant needs nothing more than a death certificate to re-title the property into his or her individual name.

Disadvantages

The disadvantages to joint tenancy are that it is not a foolproof way to avoid probate and it does not ensure that the beneficiaries you wish receive assets. As discussed above, joint tenancy does not always mean that an asset does not need to go to probate. In the event of a common disaster or the second tenant dying and neglecting to re-title, a probate proceeding will be necessary. This problem does not exist with a trust which provides for this contingency and avoids the probate.

A joint tenancy also does not ensure that the beneficiaries receive the assets the joint tenant wishes them to receive. Often times a person titles property jointly with a spouse or a child who lives nearby and assumes that person will leave the property to his or her children or brothers and sisters. This is a bad assumption to make. The old saying goes, "when people die and there is money involved, people change." The only ways to make sure the people you want to receive the property is to make them the joint tenant or to create a revocable trust. Also, a trust allows more flexibility on how to leave the property to your beneficiary. If you want them to get a certain amount over time or have it held in trust it cannot be accomplished through joint tenancy.

Possible Adverse Tax Consequences

Joint tenancy may have extremely bad estate tax consequences when the joint tenant is a surviving souse. As discussed with the AB trust, married couples should attempt to maximize the unified credit, currently $1.5 million a person. By placing a piece of property in joint tenancy with a spouse, the surviving spouse will own the property upon the deceased spouse's death. The gift of the property will count against the first to die spouse as unified credit, as well as the second to die spouse's unified credit. The tax consequence could be hundreds of thousands of dollars in taxes. A revocable trust can avoid this problem and save a large amount of money. See the discussion on AB trusts.

Joint Tenants, Creditors, and Divorce

As already discussed, joint tenants each own an entire undivided interest in the jointly owned property. This can spell disaster when the other joint tenant is an irresponsible child. Creditors may be able to attach any interest in property owned in joint tenancy. So, if an individual makes a child a joint tenant to avoid probate and the child takes a loan against that interest a creditor can go after both joint tenants. Even if the child does not have financial problems, accidents happen. Property in joint tenancy is subject to the claims of not only creditors to whom the property was put up as collateral, but to other individuals whom the joint tenant owes money to. For example, these creditors could include the victim of a car accident for which a joint tenant was found liable. This is the most dangerous aspect of a joint tenancy. Even responsible children can run into financial difficulty. A revocable trust avoids this problem.

In the event of a joint tenant's divorce, both joint tenants' interest can be attached by the divorce court for the spouse of one joint tenant. Again, divorce and financial problems happen to the best and most responsible people. There is no reason it should affect an individual's estate plan. That is why an individual should place property in a revocable trust and not in joint tenancy. The property is vulnerable to the claims of creditors and former spouses in the event of divorce.

Beneficiaries May Not be Who You Want

With joint tenancy, the tenant who dies last controls where the property goes. Since the survivor controls where the asset eventually ends up, there is no way to control where the property goes upon the first tenant's death. The second joint tenant controls where the property goes after the first tenant passes away. The second tenant can sell the property, spend it if it is a bank account, or keep it and pass it on to his heirs. The first tenant to die has absolutely nothing to say about what happens with the property once he is dead. People need to consider this when they create a joint tenancy, especially when it is with a spouse from a second marriage. The children could get nothing.

Loss of Control

While both tenants are alive, either joint tenant has complete control over the property. So, when an individual owns property and decides to attempt to avoid probate by making a child a joint tenant of the property that child has as much control over the property as the original owner. The joint tenant can spend all of the money in a jointly held account, take a loan out against a jointly owned piece of real property, or sell jointly owned stock. Joint tenancy effectively relinquishes control of property to the new tenant. The new tenant has the same rights of ownership as the original tenant. The original tenant has no recourse and cannot undo the transfer of ownership interest. This is especially true for real estate. If there is a joint tenant on a home, that home cannot be sold without permission by the joint tenant. This can cause serious family controversies and is not necessary if the individual just took the time to do a trust.

Once the first tenant passes away, that individual has no control over the property he or she once held in joint tenancy. The survivor has the right do whatever he wishes with the property. The remaining tenant may sell the property, gift it to another individual, or leave the property for his or her heirs. This is important for an individual to consider when making a gift of his or her property by making a child a joint tenant. That child can do what he wishes with the property.

ITF or POD Accounts

In trust for (ITF) accounts, or pay on death (POD) accounts, are an effective tool to keep bank accounts from probate. But, the ITF accounts are not foolproof. Under an ITF account, the creator of the account manages and owns the account during his or her lifetime. The creator simply names a beneficiary who will receive the assets in the account upon the death of the creator. The beneficiary has no right to the assets held in the account until the creator passes away.

Definition and How it Works to Avoid Probate

An ITF account avoids probate because the account has a designated beneficiary. The beneficiary takes the assets outside of probate because the asset by its title has a beneficiary and the holder of the account has instructions on what to do with the account. All that the beneficiary needs to do is to show the financial institution, where the asset is held, a death certificate. The only time an ITF account would need to go to probate is if the designated beneficiary was deceased and no contingent beneficiary was named.

Advantages

An ITF account has several advantages; it avoids probate if it is set up properly, it is inexpensive and easy to set up. All that is required is to contact the financial institution and re-title the account. As discussed above, an ITF account avoids probate because the account has a designated beneficiary. The beneficiary takes the assets outside of probate because the asset is the beneficiary’s by operation of law.

ITF accounts have a significant advantage over joint tenancy in that creditor’s claims cannot attack ITF accounts. Unlike joint tenancy, because an ITF account is not owned by the beneficiary, the beneficiary’s interest in the account cannot be attached by creditors while the creator of the account is alive. The account could be attached once the creator dies because the beneficiary then owns the account. Remember that a revocable trust can contain a spendthrift clause that prevents creditors from attaching a beneficiaries interest. This is another example of why a revocable trust is a superior estate planning tool to joint ownership or ITF accounts.

No Loss of Control

The creator of an ITF account has control of any assets in the account while living. The beneficiary of the account has no control of the assets in the account until the creator is deceased. The beneficiary does not need to know about the existence of the account. Many people do not tell their children that they have set up ITF accounts for them because of the potential for problems.

The ITF account is very different from joint tenancy when it comes to control. Under joint tenancy, each joint tenant has the ability do whatever they wish with the entire asset. With an ITF account, the creator of the account is the owner and sole controlling party. The beneficiary only stands to gain if the assets in the account exist at the time of the creators death. The beneficiary has no control, unlike a joint tenant.

Disadvantages

The only real disadvantage to the ITF account is that it is not foolproof. An ITF can result in a probate if the account is not set up correctly. The account must have a designated beneficiary and a contingent beneficiary to be effective. Even then, if both are deceased at the time of the creator's death the account must go to probate. The ITF is usually an effective tool, but it is still not as effective as a revocable trust.

People often neglect to consider the possibility that their children could pass away before them. With an ITF account, this could be problematic if the child is the designated beneficiary because the account then becomes a sole name asset because there is no beneficiary. People creating ITF or POD accounts need to name contingent beneficiaries and name new beneficiaries if a named beneficiary passes away.

Problem with Beneficiaries

The problem with an ITF account and beneficiaries is that the beneficiary named on the ITF account is not obligated to share the money with other beneficiaries. People often set up ITF accounts assuming that the named beneficiary will "do the right thing" and share the money with individuals not listed on the account. The creator of the account only lists one beneficiary for the sake of simplicity, but instructs the listed beneficiary to share the money with others. The listed beneficiary is under no legal obligation to do so, however.

If Beneficiary Dies Before Creator

When the designated beneficiary dies before the creator of the account, the creator needs to appoint another beneficiary. Another beneficiary needs to be named even if a contingent beneficiary is named. The existence of a beneficiary is the only way that an ITF account avoids probate. Therefore, a new beneficiary must be named if a beneficiary passes away before the creator of the account. A revocable trust should already address this problem.

If Beneficiary is a Minor or Too Young to Receive Money

Most states have laws that require a guardian or custodian be appointed over assets received by minor children. These laws are designated to protect a child from himself as well as others. Children are obviously not accustomed to dealing with money, especially large amounts. Guardians cost money. A court appointed guardian or custodian reports to the court regarding the asset received by the minor. The child cannot spend the money without clearing it with the guardian and the court.

There are definitely benefits to having a court appointed guardian. Someone is accountable for managing the assets received by a minor. But, this could be accomplished by leaving the asset to the child through a trust to be held in another trust for the child's benefit. The revocable trust would save money and the settlor could decide who the trustee would be and how the money would be distributed, instead of leaving the determination up to the court.

Not Available with all Assets

Not all assets can be set up as ITF accounts. Only financial accounts and some stocks can be owned as ITF accounts. Real property cannot be set up as an ITF or POD. ITFs are actually what is known as Totten trusts. A Totten trust is essentially a revocable trust dealing with an individual asset. The law allows this for certain assets, but not for others. Because not all assets can be distributed upon death by setting them up as POD accounts, another estate planning tool must be used if an individual owns any of the types of assets that cannot be owned as POD accounts. This is why a revocable trust is a far superior tool than an ITF account. The revocable trust can hold any type of property. The revocable trust also guarantees that the assets placed in it are not subject to probate if titled correctly. No other estate planning tool is as reliable and flexible as the revocable trust.

Possible Adverse Tax Consequences

Much like property owned by joint tenants, ITF accounts can result in adverse tax consequences. ITF accounts may have extremely bad estate tax consequences when the beneficiary is a surviving spouse. As discussed with the AB trust, married couples should attempt to maximize the unified credit, which is currently $1.5 million a person. By placing a piece of property in an ITF account with a spouse named as the beneficiary, the surviving spouse will own the property upon the deceased spouse's death. The gift of the property will count against the unified credit of the first spouse to die as well as the unified credit of the second to die. The tax consequence could be hundreds of thousands of dollars in taxes. A revocable trust can avoid this problem and save a large amount of money.

Beneficiaries on IRA and Life Insurance

IRAs (individual retirement accounts) are tax deferred savings plans that are allowed by the IRS. By placing money in an IRA, an individual can defer the income tax liability of that money until the money is distributed. The money in an IRA passes outside of probate as long as the IRA lists a living beneficiary. If the beneficiary listed and the contingent beneficiary are both deceased, the assets in the IRA must go to probate. IRAs have special rules for spouses that make it advantageous to name one's spouse as the beneficiary. These special rules are called "roll-over" provisions and they allow a surviving spouse to save a great deal of money in taxes. IRAs with living beneficiaries do not go through probate.

Life insurance is a concept many people are familiar with. Life insurance comes in many different forms and varieties. The basic nature of life insurance is that an individual takes a policy out insuring his or her life. Upon the death of that individual, the beneficiaries listed on the policy receive a death benefit from the insurance company. The death benefit passes to the beneficiaries outside of probate. However, there are many types of life insurance and not all of them are as simple as an individual dying and a beneficiary receiving a death benefit.

How it Works

The beneficiary under an IRA or life insurance policy receives the assets gifted through the IRA or life insurance policy outside of probate. Life insurance proceeds are not taxed to the beneficiary, but do count against the unified credit of the decedent. Therefore, life insurance proceeds are subject to estate tax if the decedent's estate is valued at over $1.5 million, under the current rules. The life insurance company writes a check to the beneficiary once it receives a death certificate for the individual whose life was insured. Insurance companies may require additional forms be filled out, but the process is relatively simple. Remember that there are different types of life insurance policies, such as second to die, that do not work the same way as the example above.

IRAs work differently than life insurance policies. Once an individual passes away owning an IRA, there is a complex set of rules that determines how the assets in the IRA are to be distributed. The simplest rule is when the designated beneficiary of an IRA is the decedent's surviving spouse then the spouse can simply re-title the IRA into his or her name and treat the IRA as his or her own. The roll over, as it is called, has significant tax advantages. One such advantage is that the assets are subject to the unlimited marital deduction for the purposes of estate taxes. Additionally, the spouse could defer the income tax liability even longer especially if the surviving spouse is younger than the decedent. The surviving spouse's age would then be used in the calculation of the minimum distribution.

When the beneficiary of an IRA is not the surviving spouse of a beneficiary, the beneficiary is liable for the income tax liability deferred by the original owner as they receive the distributions. The IRS requires that the beneficiary take certain minimum distributions. The rules for determining the minimum distributions are complex and are not vital to this discussion.

Advantages

The main advantage to life insurance policies and IRAs is that they are relatively simple to set up and, if done correctly, pass assets on to beneficiaries outside of probate. Life insurance policies can be useful in estate planning because they pass cash on to beneficiaries who may need the money for everyday expenses and bills. Life insurance is simple, easy, and works to avoid probate if set up correctly.

An IRA has several distinct advantages. An IRA defers income tax liability on the money placed in the IRA. This can save a person a large amount of money in taxes over a lifetime. An IRA also avoids probate if set up correctly.

A Trust Is Not Needed

Assets left to a designated beneficiary through an individual retirement account or a life insurance policy do not need to go through the probate court upon the original owner's death. There is no need to place a life insurance policy or an IRA account into a revocable trust if they are set up correctly. In fact, with an IRA a revocable trust could cause a tax liability that would not have otherwise existed. It is important to understand the IRA rules if an individual is planning on creating an IRA.

Passes Directly to Beneficiaries

Assets passed on to beneficiaries through an IRA or life insurance policy go directly to the beneficiary. The beneficiary will receive the assets outright and free of trust. For most beneficiaries this is fine. The beneficiaries can use the money for whatever they see fit. They can pay bills, pay for a child's education, or buy a house. For the most part, beneficiaries receiving assets are not a problem.

However, in several instances a beneficiary receiving an asset outright is not such a good idea. A beneficiary could be a spendthrift, an irresponsible person, a gambler, a minor, or an individual with a substance abuse problem. These circumstances are not good for IRA and life insurance distributions. The individual could spend the money almost immediately, worse yet is what he could spend it on. It is not a person's obligation to protect his or her children forever, but there is no need to make a bad situation worse. Giving a large sum of money to a person with a gambling problem is like throwing the money away and giving money to a drug addict is like giving a loaded gun to a suicidal person.

Must Go Outright To Beneficiary

Assets passed to a beneficiary by means of an IRA or life insurance policy must go directly to the beneficiary. The assets cannot be held in trust regardless of the wishes of the owner of the IRA or life insurance policy unless the trust is listed as the beneficiary.

The assets from an IRA or life insurance policy can be left to a revocable trust as beneficiary, but as discussed above there are drawbacks to doing so. Leaving the assets to a revocable trust as beneficiary is the only way to leave the assets in trust for beneficiaries. The assets will be distributed to the trust and then distributed according to the terms of the trust. If the trust designates that the assets are to be continued in trust for the beneficiaries, then the assets can be held in trust.

Possible Adverse Tax Consequences

Much like property owned by joint tenants and ITF accounts, IRAs and life insurance can result in adverse tax consequences. IRAs and life insurance may have extremely bad estate tax consequences when the beneficiary is a surviving souse. As discussed with the AB trust, married couples should attempt to maximize the unified credit, currently $1.5 million a person. By placing a piece of property in an IRAs or life insurance with a spouse named as the beneficiary, the surviving spouse will own the property upon the deceased spouse’s death. The gift of the property will count against the unified credit of the first spouse to die as well as the unified credit of the second spouse to die. The tax consequence could be tens of thousands of dollars in taxes. A revocable trust can avoid this problem and save a large amount of money.

Living Trust

Disadvantages

The only disadvantages to a revocable trust are that it costs money up front to set up and it involves a considerable amount of work re-titling assets. As mentioned before, a revocable trust can cost anywhere from $200 to $3,000 dollars. A revocable trust does not need to be long and complicated to be effective.

The re-titling of assets is an unavoidable drawback to setting up a revocable trust. Assets must be re-titled into the name of the revocable trust in order to be effective. An asset not placed in the trust must go through probate if it is owned in the individual’s sole name. Re-titling takes some leg work. Every sole name asset needs to be re-titled into the name of the revocable trust. This involves contacting every institution where assets are held and informing them of your intent to re-title the assets. This takes time to write letters, fill out forms, and forward copies of the trust. The work done is minimal compared to the work that will need to be done if the estate needs to go to probate.

Chapter 13
Estate Taxes

How it works

The federal government currently taxes the estate of an individual if he or she owns assets worth over $1.5 million at the time of his or her death. This is because under federal law, an individual is only allowed to gift $1.5 million during his or her lifetime or at death. So, if an individual had gifted $1.5 million over his or her lifetime, to individuals, then any assets he or she owned at death would be taxable to the estate. Remember that an individual is also allowed to gift up to $11,000 a year to anyone he or she wishes. This is referred to as the annual exclusion and does not go into the computation of the $1.5 million amount of lifetime gifts.

State governments also pass laws that establish an estate tax. These taxes are usually in addition to the amount charged by the federal government. The state estate taxes usually occur regardless of the value of the estate. All estates that are solvent are taxed. Some states do have a minimum amount at which the estate tax begins, but that amount is much lower than $1.5 million. Some states do not have additional estate taxes. For example, Florida receives a portion of the federal estate taxes received from Florida residents when they pass away.

The federal government gives a tax credit for estate taxes for the amount of tax paid in state estate taxes. The tax credit can be significant when one considers that the estate only receives the tax credit when it is valued at over $1.5 million.

What is Taxed

All assets passed by an individual upon their death are considered in the computation for federal estate tax purposes. Life insurance proceeds, assets from a revocable trust, and ITF accounts all are subject to estate taxes.

Federal Estate Tax Return, Form 706

The federal government requires that a tax return be filed when an estate is valued at over $1.5 million. The estate tax return is called a Form 706, federal estate tax return. Form 706 needs to be filed with the IRS within nine months of the date of the decedent’s death. Form 706 is a comprehensive tax return that requires a great deal of information and is so complicated that it must be prepared by an accountant or tax attorney. The tax attorney or accountant usually works closely with the personal representative or successor trustee to obtain all the necessary information. The preparation of the Form 706 is expensive because of all the time that is necessary to prepare it. A large amount of an attorney’s fee for administering an estate is the fee associated with the preparation of the Form 706.

Form 706 is often referred to as a “snapshot” of everything owned by a decedent at the time of his or her death. Because most people do not keep a detailed record of their assets, the individual preparing the Form 706 must piece the information together. This becomes difficult because people often have assets that family members and loved ones are not aware of. People are secretive and sometimes do not want others knowing about their finances for any number of reasons. People also forget that they own small assets that may have appreciated over time. All of these factors combine to make the job of the person preparing the Form 706 very difficult.

Form 706 must contain the following information on the appropriate schedule:

- Schedule A – Real Estate
- Schedule B – Stocks and Bonds
- Schedule C – Mortgages, Notes and Cash
- Schedule D – Life Insurance
- Schedule E – Jointly Owned Property
- Schedule F – Miscellaneous Property
- Schedule G – Life Transfers
- Schedule H – Powers of Appointment
- Schedule I – Annuities

The person who prepares the Form 706 must file the first three pages of the return. The schedules only need to be filled out and attached if the decedent owned the appropriate property.

Tax Rates and Unified Credit

The federal government allows an individual to gift, during his or her life and at death, up to $1.5 million. That amount is referred to as the unified tax credit. The unified tax credit is scheduled to increase over the next several years. It should be noted that the current law is scheduled to eliminate the tax in the year 2010. At that point, there will no longer be a federal estate tax. Many people believe that we will have a new law in effect by then. It is hard to image that the federal government will go without the billions of dollars in tax revenue that are generated every year by the federal estate tax.

Year	Applicable Credit	Applicable Exclusion
2002-2003	$345,800	$1 million
2004-2005	$555,800	$1.5 million
2006-2008	$780,800	$2 million
2009	$1,455,800	$3.5 million
2010 and beyond	Estate Tax Repealed	No Estate Tax

The tax rate for an estate is much higher than other tax rates. Income tax and capital gains rates start at significantly lower rates than the federal estate tax rate.

It is important to understand how the federal estate tax works because it is much different than the way income taxes work. The estate tax is imposed on the transfer of the taxable estate of a decedent.

As discussed earlier, a taxable estate is any estate where the decedent passed or is passing over $1.5 million as gifts. As the rate schedule below will illustrate, the federal government is giving a tax credit of $345,800. The $345,800 is the tax that would be due on a $1.5 million estate. The federal government never charges the $345,800, it is given as a credit. The schedule below lists the tax liability before that $345,800 is deducted.

Amount	Tax Liability
Over $1 million but not over $1.25 million	$345,800 plus 41% of the excess of amount over $1 million
Over $1.25 million but not over $1.5 million	$448,300 plus 43% of the excess of amount over $1.25 million
Over $1.5 million but not over $2 million	$555,800 plus 45% of the excess of amount over $1.5 million
Over $2 million but not over $2.5 million	$780,000 plus 49% of the excess of amount over $2 million

How to Determine Net Worth

The net worth of an estate is the value of all the assets owned by the decedent at the time of death. All of the property owned by the decedent is considered. The net worth of an individual also takes into account any liabilities the decedent owed at the time of death. Debts are deducted from the amount of assets owned by the decedent at death when computing the taxable estate. The net worth of an estate is referred to as the gross estate. The gross estate is valued at the fair market value on the decedent's date of death or, if elected, on the alternate valuation date, which is six months after the date of death. The IRS allows you to use the alternate valuation date if the total estate is worth less on the alternate valuation date than on the date of death. The amount of taxable gifts made after 1976 is added to the taxable estate. The taxable estate also includes all tax credits and deductions from things like attorney's fees, charitable deductions, and state death taxes. Schedules J through T on the Form 706 list all tax credits and exclusions. Below is a list of credits and exclusions accompanied by the corresponding schedule in which it is found on the form 706:

- Schedule J – Funeral and Administrative Expenses
- Schedule K – Debts
- Schedule L – Losses and Non-Claim Expenses
- Schedule M – Marital Deduction
- Schedule N – Employer Stock Ownership Plan
- Schedule O – Charitable Deductions
- Schedule P – Credit for Foreign Death Taxes
- Schedule Q – Credit for Tax on Prior Transfers
- Schedule R and R-1 – Generation Skipping Transfer Tax
- Schedule S – Estate Tax and Excess Retirement Accumulations
- Schedule T – State Death Tax Credits

New Tax Law

As discussed earlier, the federal government has changed the estate tax laws. The new law increases the unified credit amount to $1.5 million for 2002 and raises it incrementally until it reaches $3.5 million. In 2010, the new law is subject to a “sunset” provision whereby the law repeals itself and reverts back to the 2001 rules. This is highly unlikely to happen because most experts expect the law to be changed by then. This law seems to be a temporary solution to an ongoing debate and problem. People have been pushing for the government to eliminate the so called, “death tax,” for years. However, the federal government receives billions of dollars in revenue from the tax. Most people in the field do not see how the government could manage to do without the revenue source, especially with the recent economic instability.

Year	Applicable Credit	Applicable Exclusion
2002-2003	$345,800	$1 million
2004-2005	$555,800	$1.5 million
2006-2008	$780,800	$2 million
2009	$1,455,800	$3.5 million
2010 and beyond	Estate Tax Repealed	No Estate Tax

Review Existing Estate Planning for New Tax Law

The new estate tax law will have little effect on the average person. Most people are not worth over $1.5 million so they do not need to worry about federal estate tax issues. They may be liable for state death taxes, but that is a matter for their state legislature. As for individuals with over $1.5 million in assets, their estates will be subject to the new tax law and rate schedule. If they have surviving spouses, they should consult an estate planning attorney regarding an AB trust. The AB trust could be used to maximize the unified credit of the two married individuals and potentially save thousands of dollars in tax liability.

Individuals who currently have AB trusts that are funded with assets worth much less than $1.5 million may also wish to consult an estate planning attorney. The new law may make their estate plan obsolete because there is no need to create a residuary trust to maximize the unified credit when the estates together are worth far less than the new unified credit. With the recent increases in the unified credit, many people have AB trusts that are protecting assets that do not need to be protected.

Some estate planning attorneys are recommending that people keep their AB trusts because the new tax law repeals itself in 2010. No one knows what could happen, so planners are suggesting that people keep things the way they are. The only real reason to change the AB trust is if the spouse needs the money passed to him or her free of trust or do not want assets held in a residuary trust. It is important to remember that with second marriages AB trusts and QTIP trust serve a special purpose. They prevent a surviving spouse from spending all of the money left to the him or her so the children of the deceased receive some of the assets.

The people who really benefit from the new tax law are the individuals who have between $675,000 and $1.5 million in assets. These estates will not be subject to estate tax where they once would have been.

Chapter 14
Basic Estate Planning

Use of Unified Credit With AB Living Trust

An AB trust is actually not a trust, they are two separate revocable trusts set up for a married couple. The AB trust is used to maximize the unified tax credit. The unified tax credit is a tax law that states that an individual can gift during his lifetime or at death a specified amount. That amount is currently $1.5 million. The amount will be going up over the next few years.

Year	Unified Credit/ Exclusion Equivalent
2002-2003	$1 million
2004-2005	$1.5 million
2006-2008	$2 million
2009	$3.5 million
2010 and beyond	No Estate Tax

The AB trust maximizes a married couple's unified tax credit by creating a residuary trust upon the death of the first spouse. The trust of the first spouse to die directs that the residuary trust be funded with the maximum amount allowed to be passed free of tax and be allocated to the residuary trust held for the benefit of the surviving spouse. This means that the first spouse uses close to the $1.5million unified tax credit. This prevents the money from going to the surviving spouse's taxable estate. Since the money is in the residuary trust, when the surviving spouse passes away another $1.5 million can be passed along to beneficiaries free of estate tax. The residuary will pay out income and principal to the surviving spouse during his or her lifetime and upon his or her death, the trust will pay out to the beneficiaries designated by the original settlor. The money left over after the $1.5 million is used to fund the residuary trust will pass either directly to the surviving spouse or another trust can be created.

An AB trust is often referred to as a residuary trust or credit shelter trust. This is because the AB trust creates a residuary trust upon the death of the first spouse to "shelter" the unified credit. These terms should not be confused with the term marital share. The marital share is the portion in excess of the residuary trust. The marital share can either be distributed outright to the surviving spouse or held in trust. When the marital share is held in trust the trust is called a QTIP, or qualified terminable interest property trust. This second trust is held for the surviving spouse's benefit but the surviving spouse is not allowed to invade the principal. The QTIP trust prevents the surviving spouse from spending all of the assets in the marital share, which would prevent the deceased spouse's heirs from inheriting it.

Often, especially with second marriages, the money in excess of $1.5 million is held a trust so the children of the first spouse to die cannot be disinherited. This type of trust is referred to as a QTIP trust, or qualified terminable interest property trust. QTIP trusts are often used in conjunction with AB trusts to insure that the children from a decedent's first marriage receive the assets from the trust. These are often necessary because without such a trust the surviving spouse could simply spend all the money in the residuary trust and the deceased spouse's children would receive nothing.

The following charts show how the AB trust works:

> Imagine a couple with $2 million in assets. The couple has created revocable trusts for each other's benefit. Each trust is funded with $1.5 million. The trusts create residuary trusts for each other's benefit, upon death, funded with an amount as close to the unified credit as possible.

If Spouse #1 passes away:

Spouse #1 AB Revocable Trust $1.5 million	**Spouse #2 AB Revocable Trust $1.5 million**
Spouse #1 passes away Revocable Trust Funds Residuary Trust	
Residuary Trust for Spouse #2's Benefit $1.5 million held in trust for children's benefit NO TAX DUE! Spouse #1 uses $1.5 million Unified Credit.	Spouse #2 Revocable Trust $1.5million

Now if Spouse #2 passes away:

Residuary Trust $1.5 million	**Spouse #2 Revocable Trust $1.5 million**
Spouse #2 passes away Residuary Trust Passes to Children $1.5 million NO ESTATE TAX DUE!	Spouse #2's Revocable Trust Passes to Children NO ESTATE TAX DUE! Spouse #2 uses $1.5 million Unified Credit

Imagine now that the couple with $2 million in assets did not create the AB trust and simply had two revocable trusts that distributed assets to the survivor of the two upon death.

If spouse #1 passes away:

Spouse #1 Revocable Trust $1.5 million	Spouse #2 Revocable Trust $1.5 million
Spouse #1 Passes Away Spouse #1 Uses all Available Unified Credit	$1.5 million Passes to Spouse #2 Free of Trust

Now if Spouse #2 passes away:

	Spouse #2 Revocable Trust $1.5 million
	Spouse #2 Free of Trust $1.5 million Spouse #2 Revocable Trust $1.5 million

Spouse #2’s estate has only $1.5 million of unified credit and $2 million in assets. Spouse #2’s estate will be taxable. The estate did not need to be taxable. If the couple had created an AB trust neither estate would have been taxable and the result would have been the same. The only difference is that Spouse #2 could only invade the principal in the residuary trust for his or her health, maintenance, and welfare.

Splitting Assets

The key to any revocable trust is that it is funded. Funding an AB trust is even more important than funding an ordinary trust. The AB trust will not work to maximize the unified credit if it is not funded. In order to fund an AB trust, the married couple must split their assets or divide them evenly. The married couple must split the assets evenly because it will insure that the unified credit will be maximized. If one of the spouses has more assets than the other, the spouse to die first could be the one with fewer assets. If the spouse to die is the one with an underfunded trust, that spouse would not be using all of the available unified credit. When the second spouse passes away, since the second spouse’s trust was overfunded, the second spouse’s estate would be taxable or liable for more taxes. This could be avoided or mitigated (if the estate would have been taxable anyway it will still reduce the taxes).

The simplest way to split assets is to divide them equally between the two married persons. This is not always as easy as it sounds. Some assets are not easily divided. A married couple could have $2.5 million in assets, but $1.5 million could be the value of their home. This means that one of the trusts would have only the home and the other spouse’s trust would have to contain the other assets. This would mean that the trusts were not funded equally. It also would mean that one of the trusts would contain all of the liquid assets and the other trust would contain the home, not a liquid asset.

Ideally, the math would work out and both trusts would be funded equally. If the math does not work out, the assets need to be divided as close to equally as possible. It is important to understand that any assets placed in a trust are under the control of the trustee of that trust. If the spouses wish to both control an asset that is placed in one of the trusts, the other spouse must be named as a co-trustee of that trust. This enables both spouses to control the asset. Some people do this with all of their asset so that both spouses can control all of the assets.

One Trust Versus Two Trusts

It is possible to create an AB trust in one single document. The single document is be a joint revocable trust. The joint trust has the same provisions as the two separate trusts discussed earlier. The joint trust states that upon the death of either of the spouses a residuary trust will be established. That residuary trust will be funded with an amount as close to the unified tax credit as possible. The residuary trust will be held for the surviving spouse's benefit with the right to invade principal for health, maintenance, and welfare. This trust would accomplish the same results as the two separate trusts described earlier.

Then, why create two separate trusts? Two separate trusts are normally created for clarity and ease. The IRS has taken a position in the past that a joint revocable trust that creates a residuary trust to maximize unified credit is ineffective. The IRS does not usually challenge the validity of the joint trust, but they could. The IRS could claim that the assets were jointly owned by the two settlors and therefore upon the passing of the first spouse, the second spouse would own all of the assets. This would defeat the purpose of the AB trust and would mean that the couple would only have $1.5 million in unified credit instead of $2 million. So for the sake of clarity, most estate planners simply create two trusts. Since one spouse is the settlor of one trust and the other spouse is the settlor of another there is no confusion about the ownership of the assets. The AB trust will then work to maximize the unified credit.

The creation of two trusts instead of one trust for an AB trust makes the administration easier. It is clear which trust owns which asset. The spouses can divide the assets while living and plan accordingly instead of splitting the assets upon the death of one of the spouses. Splitting the assets after the death of one spouse can be difficult because not all assets can be divided. Assets like CDs, real property and annuities are difficult, if not impossible, to divide. With two separate trusts, the assets are already divided.

Funding Each Trust

Each of the two trusts in the AB trust must be funded for the AB trust to effectively maximize the unified credit. Since the unified credit is currently $1.5 million, a couple creating an AB trust will usually have at least $1.5 million in assets and usually more. This means that each trust should be funded with less than $1.5 million if at all possible to maximize the unified credit. The two trusts should be funded equally until both reach $1.5 million apiece. This will insure that the trust is as effective as it can be.

The trusts in the AB trust are funded the same way as an ordinary revocable trust. The settlors must contact the institutions where the assets are held and inform them that they wish to re-title the asset into the name of a revocable trust. The institution should be given the name of the trust that is to hold each asset. It is up to the settlor to decide which assets go in which trust. An attorney or accountant can often be helpful in determining which assets should be placed in which trust. All assets are re-titled the same way as they are with an ordinary trust. This means that property, stocks, brokerage accounts, and bank accounts are all re-titled the same way as discussed in *Chapter 8 Funding A Trust*.

Gifting Annual Exclusion

The federal government taxes gifts made from one individual to another. However, an individual can make an $11,000 gift to anyone each year free of tax. This gift can be made to more than one person. This gift is called the annual exclusion and will be increasing over time. In addition to gifting $11,000, the annual exclusion includes gifts made directly to an educational institution or a medical institution. The annual exclusion amount is not subtracted from an individual’s unified tax credit. Remember, the unified tax credit allows an individual to gift up to $1.5 million during his or her lifetime or at death free of estate tax. This gift can be a useful tool in lowering estate taxes.

It should be mentioned that the individual receiving a gift is not the one responsible for the gift tax liability. The individual making the gift must pay the gift tax. Most people do not pay the gift tax. They simply count it against their unified credit. This is done by filing a Form 709 federal gift tax return. The Form 709 gift tax return must be filed for every gift over the annual exclusion amount. So, if an individual wishes to gift $20,000 to a grandchild, they must file a Form 709 for a $9,000 gift. The individual can elect to pay the tax liability for a $9,000 gift or can count it against their unified credit, unless they have already used the entire unified credit amount.

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Chapter 15
More Sophisticated Estate Planning

For estates greater than the unified credit amount (currently $1.5 million), many people make gifts of money to fund insurance policies to help pay the tax liability. Today, a wide range of insurance policies are available to solve a number of estate planning problems. Insurance can be used as a wealth replacement tool, to pay estate taxes, or as an investment vehicle.

Leveraging Gifts With Life Insurance

Insurance is most effective in estate planning when it is used to maximize gifts. Since an individual can gift $11,000 a year as part of the annual exclusion and up to $1.5 million during his or her lifetime, under the unified tax credit, there are a multitude of estate planning options to leverage that gift into a large life insurance policy. Many of these estate planning options involve insurance.

Second to Die Policy

A second to die policy is a life insurance policy that insures the lives of two people. The policy only pays a death benefit upon the death of the second insured party. The purpose of the second to die policy is that it is cheaper to purchase the policy and, if the family did proper estate planning, the taxes are not due until the second death. The proceeds from the policy can then be used to pay the tax liability. This can be very helpful.

The proceeds from the life insurance are subject to estate taxes. To prevent this, the ownership can be transferred to the children or to an irrevocable life insurance trust. The policy will provide liquid assets because many times assets must be sold to pay the estate tax liability or removed from the investment they are currently in.

Irrevocable Life Insurance Trust

An irrevocable life insurance trust (ILIT) is an irrevocable trust that is funded with life insurance. The settlor of an ILIT creates the trust, but for tax purposes is not allowed to be the trustee of the trust. If the settlor is the trustee, the IRS will look at the trust as though it was owned by the settlor and the trust will be included in the settlor's estate. Most people name the beneficiary of the trust as the trustee because the beneficiary of the trust has the option of cashing in the life insurance at any time. A settlor could just as easily name his or her surviving spouse as trustee. This is common when the beneficiaries are minors. The beneficiary can cash in the life insurance policy because he or she owns the policy. In order to make the settlor's purchase of the life insurance a completed gift, the beneficiary of the trust must have the option of cashing the policy in every year when the gift is made.

The settlor of the ILIT gifts the amount of the premium of the insurance policy every year to the trustee. Remember, the premium is part of the annual exclusion so there must be enough beneficiaries to cover the exclusion.

The ILIT is a wonderful tool for spending down a taxable estate. Many people do not need millions of dollars to live their daily lives, especially many frugal seniors. So, instead of holding on to assets that will be taxed, they can gift them during their lifetime. The gift can be given outright or held in a trust for different reasons. An ILIT is a trust that enables the settlor to gift down his or her estate and leave assets in trust.

Irrevocable and Out of Estate

Since an ILIT is an irrevocable trust, the ILIT is not included in an individual's estate for estate tax purposes. An irrevocable trust is a completed gift. A completed gift is not included in an individual's estate for estate tax purposes. If the settlor kept the annual premium for the insurance in the trust under $11,000 per beneficiary, the ILIT will not count against the settlor's unified tax credit. This is the optimum use of the annual exclusion amount and life insurance. An experienced and trusted insurance agent and tax attorney should be consulted about the wisdom in gifting over the annual exclusion amount.

Crummey Letters

A Crummey letter is the strange name given to the letter written by the trustee of an ILIT to the beneficiaries of the trust to inform them that they have the option of cashing in the insurance policy in the trust. The Crummey letter is written to give the beneficiary the option of cashing in the policy. This must be done so that the gift of the premium qualifies for the annual exclusion. The oddity of the Crummey letter is that the beneficiary of the trust is often the trustee. It is important that the beneficiary or trustee of the trust write the letter to himself. If the letter is not written to the beneficiary then the gift is not completed and there are adverse tax consequences. Many times the trustee is the parent of a minor beneficiary. It is still important the minor beneficiary receive the Crummey letter.

Qualified Personal Residence Trust

A qualified personal residence trust (QPRT) is another sophisticated estate planning technique. The QPRT is a trust where the settlor of the trust makes a gift of his or her home to a designated beneficiary. The attorney preparing the trust uses a mathematical formula with a schedule from the federal government to calculate a gift value of the property.

The property needs to be assessed to determine its value. Once the property value is determined, the attorney can determine the value of the property once it is gifted to the QPRT, which will be a different value. The property gifted to a QPRT has a diminished value because it is held in trust and subject to the settlor living in the house for a set number of years.

Discount

The QPRT has several advantages over gifting a piece of property outright. The property gifted to a QPRT has a discounted value because the property is subject to the reservation. The marketability of a piece of property is greatly diminished when someone has the right to live on it during a period of time. Therefore, the amount of the gift is significantly lower than the actual value of the home. The gift is in addition to the annual exclusion.

The value of the property gifted to the QPRT counts against the settlor's unified credit. If the settlor elects, the gift tax liability can be paid and the unified credit amount can be saved. Most people elect to use the unified credit.

The added bonus with a QPRT is that the property is no longer in the estate once the term expires. If the settlor dies during the term of the trust, the QPRT reverts to the estate of the settlor and is included in the estate. But, if the settlor survives the term of the trust, the settlor has gifted a highly valued asset at a greatly diminished value. The highly valued asset is also a home, which normally appreciates in value. Since that asset is no longer in the estate once the QPRT expires, the settlor has removed an asset that is likely to appreciate from their estate.

Rent

If the settlor of the QPRT has gifted away his or her primary residence, he or she now needs a place to live. The settlor no longer owns his or her home. What most estate planners suggest to people who have gifted their primary residence to their children is to rent it back from them. The rent paid to the children will further reduce the estate of the settlor and give the children a source of income. This is beneficial to the settlor and the child. The rent is also taxed at a lower rate as income to the child then it would be if it were in the estate and subject to estate tax. As discussed earlier, the estate tax rate is about 40 percent, which is a much higher tax rate than most people pay on their income taxes. Additionally, the children have access to the money immediately and do not have to wait until their parent dies to receive the assets.

The attorney who prepared the QPRT will usually prepare the lease for the settlor and the children. The lease will be executed upon the expiration of the QPRT. The property from the QPRT, already having been deeded to the QPRT, will need to be deeded to the beneficiaries of the QPRT. The attorney preparing the QPRT will normally prepare these deeds as well. The lease will need to be signed by all settlors and beneficiaries to be effective and executed with any formality required by the jurisdiction the property is located in. Once the lease is executed, the settlor should pay the beneficiaries a fair market rent.

Family Limited Partnership

A family limited partnership (FLP) is an entity created under the limited partnership laws of specific states. It is another method of gifting assets out of an estate with an IRS value much less than the actual value of the asset.

The FLP allows you to retain, essentially, indirect control over assets or shares of the partnership that you have gifted to children, grandchildren, or other individuals. While centralized management and control are benefits in the establishment of the partnership, the additional benefit of limited exposure to personal liability with respect to the assets of partnership should not be overlooked.

Structure, Creation, and Establishment

The basic structure of the partnership requires that there be at least both:

- One general partner (i.e. who owns as little as a one (1 percent interest in the partnership)
- One limited partner

Before establishing the partnership you must decide if your children will be contributing to the partnership as general partners. Generally, the general partner is a corporation or limited liability company with you, or you and your children, owning shares in the corporation in a manner which allows you to maintain control over the assets of the partnership. Even trusts for the benefit of your children may own the stocks or other interests in the corporation or limited liability company which is the general partner. The general partner makes all of the decisions regarding the partnership's management and the limited partners, for the most part, are not entitled to participate with the management.

Assets of the Family Limited Partnership

Generally, assets are transferred to the limited partnership in exchange for general (controlling) and limited (non-controlling) partnership interests. You may then gift the partnership interests to your children, grandchildren, (or trusts established for their benefit), or any other individuals you wish to benefit with gifts of the partnership interests. The gifts of the percentages of the interests are generally those which qualify for the gift annual exclusion ($11,000 per person or $22,000 if your spouse were to join in the gift). You may also choose to gift the full fair market value of your available lifetime unified credit (up to $1 million for the year 2002, depending on whether you have made any other taxable gifts during your lifetime).

When the partnership interests are valued for gift tax purposes, discounts are available for the lack of marketability and lack of control associated to the interest of shares in the partnership that are gifted. Remember, non-controlling, or limited, partnership interests have a reduced value since the limited partner cannot participate in the management of the partnership and the interest cannot be sold in an open market. The discounts usually range between 20 percent and 50% percent in the aggregate depending on how the FLP is set up. Therefore, an appraisal is necessary to determine the valuation of the interests at the time the gifts are given. The cost of the appraisal should be given consideration as it will be necessary when you choose to make gifts so that you may gift the appropriate number of shares to correlate with the annual exclusion or unified credit.

Lack of Marketability and Associated Discounts

The discount given on the value of the shares is directly related to the lack of control associated with the shares gifted. This is based upon the notion that an "arms-length" buyer would pay less for the non-controlling interests in an entity then he or she would pay for outright ownership and control of the underlying assets it owns. Again, these discounts usually range between 20 percent and 50 percent in the aggregate. The lack of marketability discount is composed of generally two components:

- First, as you may expect, there is an absence of a market of ready, willing, and able third-party buyers to purchase these interests with limited control.
- Further, state law and the limited partnership agreement itself often restrict a limited partner's ability to withdraw from the partnership. This may be viewed as a "lock-in" discount.

The restrictions reduce the purchase price of limited partnership interests sold in an arms-length transaction. As a result, these restrictions have a direct effect on value. However, these types of restrictions must be disregarded unless they are no more restrictive than those that would otherwise apply under state law.

Effect of Gifting Limited Partnership Interests

The effect of gifting limited partnership interests may be illustrated by the following example:

Assume that a one-third discount is available for lack of control and marketability, etc. as discussed above. Also assume that you are willing to use your available lifetime unified credit exemption of $1.5 million in gifting limited partnership interests to your children or grandchildren. You could essentially transfer to your children or grandchildren, without paying a gift tax, limited partnership interests reflecting $1.5 million of an FLP's underlying assets. Indirectly, you have effectively reduced your estate by $1.5 million using your $1.5 million exemption equivalent, therefore saving tax on the extra $500,000. In addition, you and your spouse could transfer partnership interests reflecting a value of up to $16,000 of an FLP's underlying assets to each of your children and grandchildren without incurring a gift tax, utilizing the annual exclusion of $11,000.

It is also important to point out that any income or future appreciation on the gifted assets is now shifted to your children or grandchildren. This avoids the income and appreciation from accruing to you and ultimately increasing the estate taxes upon your death. Accordingly, current gifting greatly maximizes the tax savings if the gifted assets subsequently appreciate. For income tax purposes, the recipient of the gift obtains a basis equal to that of the donor's (your) basis in the property transferred. This may not be as beneficial had the asset been included in your estate upon your death as the asset would then have received a basis as the value of the asset at death. However, the tax and tax rates would be applied at the full date of death fair market value which would cause far greater estate taxes to your estate than the capital gains taxes to be paid upon the sale of the assets by the recipient, if gifted. Basically, the proper structuring of the FLP may serve to significantly reduce taxes while allowing you to maintain total control over the underlying assets.

IRS Position On Family Limited Partnerships

Please note that the Internal Revenue Service (IRS) is continuing to contest the use of FLPs to help achieve these beneficial valuation discounts because people are being far too aggressive with the use of the discounts. The IRS is more likely to contest the use of the partnership (and therefore the discounts) if the FLP does not have an apparent business purpose or holds only marketable securities. A FLP that holds assets consisting of real property (as opposed to securities solely) is more likely to pass IRS scrutiny; however, this planning is still not without risk. Most of the cases have been settled such that there has been some discounted amount allowed.

Charitable Planning

The IRS and the federal government give tax breaks to individuals who make gifts to qualified charitable organizations during their lifetime or at death. These tax breaks can be used to reduce or eliminate estate tax liability upon the death of an individual and can become an integral part of passing more assets to the family. Charitable planning benefits the estate of the deceased and qualified charities. The tax break benefits the estate of the decedent and the assets gifted to the charity benefit the charitable organization. Many of these charities may not exist if it were not for the contributions from individuals doing estate planning by taking advantage of the tax benefits associated with charitable gifting. While many people do not consider donating to charity as an alternative, because they would prefer to pass the assets on to relatives, the tax benefits can be considerable and, if done correctly, can pass more assets to the family than if no planning were done.

Charitable Remainder Trust

A charitable remainder trust (CRT) is a trust whereby an individual transfers a specific dollar value in cash, appreciated stocks, bonds or other securities, and even real estate to an irrevocable trust while retaining the right to receive an income from the trust during his or her lifetime. Upon his or her death, the trust assets pass to the named charity. This allows the individual to still benefit from the asset while removing it from his or her estate for federal estate tax purposes, avoiding the large capital gains, as well as receiving an income tax deduction.

Setting up this type of trust can create significant tax savings for an individual’s estate. The reason for these savings comes from the charitable deduction for the remainder interest in the trust upon the individual’s death. Further, he or she will receive a charitable deduction which will offset his or her income taxes in the year in which the gift was made. Any unused portion of the deduction can be carried over for a five-year period. Finally, the individual can unlock the appreciation without capital gains taxes in the form of income paid. With portions of this income the individual may fund a wealth replacement trust to replenish the gifted assets income and estate tax free.

By making the gift of the assets during your lifetime, you guarantee yourself an income stream from the assets which otherwise would not be available without a significant capital gains tax, while removing the assets from your estate for federal estate tax purposes. This therefore reduces your estate's tax liability by removing the asset from your estate.

The CRT allows you to avoid capital gains taxes on the sale of the gifted assets because the charitable trust is not required to pay income taxes. Therefore, assets that had too much appreciation and were not paying any income can now be sold to generate an income stream for life.

You may act as trustee and you may choose and replace the charitable beneficiary at your discretion. Prior to establishing the trust you will need to decide who you would have act as successor trustee if you were unable to act and who the charitable beneficiary or beneficiaries are.

Wealth Replacement/Insurance Trust

As discussed, in conjunction with the CRT, a wealth replacement/insurance trust can be established for the purpose of replenishing assets to your estate upon your death. By establishing an irrevocable insurance trust for the purpose of owning a life insurance policy on your life, you may utilize a portion of the income stream from the CRT to “gift” the value of the life insurance premiums to the wealth replacement trust. The trustee, or trustees will then pay the premiums.

So long as it was structured properly and the insurance is purchased through the trust, the insurance trust will own the life insurance policy on your life. Upon your death, the death benefit proceeds, (which may be equal to the amount you had originally gifted to the CRT) would be paid to the trust which is outside of your estate. This will avoid the inclusion of the death benefit in your estate for estate tax purposes so as to replenish those assets gifted to the CRT initially, without a gift or estate tax liability.

Prior to establishing this trust you will need to decide whom you would have act as trustee and who would be the beneficiary of the trust to receive the death benefit proceeds.

Generation Skipping Tax Planning

The federal government not only levies an estate tax against estates, other taxes may apply to the estate depending on the value of the estate and who the beneficiaries of the estate are. The generation skipping tax (GST) can be levied on an estate if certain criteria are met. Just like with the estate tax, the amount of GST tax can be reduced or eliminated if proper planning is done.

What is GST Tax?

The federal government decided years ago to begin taxing assets passed by individuals from generation to generation. When an asset passes from an individual to an heir while skipping a generation, the federal government loses the estate taxes it would have received from the generation that was skipped. For example, when a grandparent passes assets to a grandchild the federal government loses the tax it would have received if the grandparent had passed the asset to the parent and then the parent had to pass the asset to the grandchild. The federal government would prefer to tax the assets twice rather than once. So, the government initiated the generation skipping tax to make up for the lost taxes.

The generation skipping tax is a one rate tax, or flat tax, set at 55 percent. The tax applies to transfers to skip persons made during life and at death. A skip person is an individual assigned to a generation that is two or more generations below the individual making the transfer. A trust can be the skip person if all of the beneficiaries are skip persons. The most common example of a skip person is a grandchild. Often, grandparents who have wealthy children see no need to leave them large amounts of money. This is especially true when their grandchildren are responsible adults and could use the money to make their lives easier (such as paying off student loans or a mortgage).

Exemption

The generation skipping tax does not apply to transfers that are under $1.1 million. The $1.1 million is referred to as the GST exemption. The GST exemption can be used during an individual’s lifetime or at death. Much like the unified tax credit, the GST exemption applies to the individual making the transfer during his or her lifetime or at death. The amount does not increase due to the number of individuals to whom gifts are. The exemption is $1.1 million if the transfer is made to one grandchild or 20 grandchildren.

Annual exclusion gifts (under $11,000 to individuals) are not counted against the GST exemption amount. This is also similar to the unified tax credit and the way it works in combination with the annual gift exclusion.

It should be noted that the GST tax is added to the estate tax when both taxes apply. In some instances, the combination of GST tax and the estate tax can result in a combined rate over 70 percent. This is a good indication that some planning should be done to attempt to maximize the GST exemption and avoid unnecessary tax liability for an estate.

Generation Skipping Trust

Trusts that can be set up to avoid generation skipping tax problems. One such trust is a generation sipping trust. The idea behind a GST trust is that the assets are held in trust for the benefit of an individual’s children. The trust is set up for the exemption amount and provides income or principal to the child or children during their lives and then passes to the grandchild or grandchildren. If the trust is established correctly, the trust is not included in your child’s estate for estate tax purposes and the assets will not be subject to GST tax because of the exemption. The details of the trust should be discussed with an estate planner to insure that there is no unexpected tax liability.

Other Considerations

Many people have the idea that they would like to pass assets on to their great grandchildren and beyond to assure financial stability for future family members. This is usually done by what is referred to as a dynasty trust. A dynasty trust holds assets in trust for future generations and pays assets out according to the settlor’s specifications. Since the beneficiaries of the trust are skip persons, the trust will be subject to GST tax if the trust value is over $1.1 million, the GST exemption. It stands to reason that anyone creating a dynasty trust would be leaving a large sum of money because the cost to create and administer the trust could be tens of thousands of dollars over decades. The fees would be cost prohibitive and the beneficiaries would be receiving no money unless the trust was funded with a large sum of money.

The GST only applies once per skip, regardless of how many generations are skipped. So, if a dynasty trust was set up to skip three generations, the GST would only apply twice. There is another problem with the dynasty trust, however, the trust is usually invalid due to many state laws. Most states have adopted laws called the rule against perpetuities. These laws prevent individuals from tying up assets for decades by controlling them through a trust. It is important that the estate planner advise clients about applicable state laws that may make certain goals difficult or impossible to achieve.

Chapter 16
Living Trust Administration After Death

When an individual passes away owning assets in a revocable trust, the trust needs to be administered according to the provision that states what is to be done upon the settlor's death. The death of the settlor of a trust can result in any number of different circumstances.

If the settlor was a co-trustee with his or her spouse of as joint trust, the trust will basically continue as though nothing has changed. The surviving co-trustee only needs to provide death certificates to the institutions where trust accounts are held to re-title the account. The surviving co-trustee will then become the lone trustee of the trust.

If the settlor is the lone trustee of a revocable trust, the successor trustee will take over as the trustee of the trust. The successor trustee's job will be to administer the trust according to the "upon death of the settlor" provision.

If the revocable trust of the decedent is an AB trust and is designed to set up a residuary trust, the successor trustee's job is to fund the residuary trust and to distribute the rest of the assets according to the terms of the trust. The successor trustee's job is not over upon the distribution of the assets.

The successor trustee will continue as the trustee of the residuary trust. As trustee of the residuary trust, the successor trustee will be required to manage the assets in the trust, file a form 1041 tax return every year, and provide for the surviving spouse from the trust as needed. The successor trustee is entitled to a fee for these duties. The successor trustee is usually the surviving spouse so he or she is usually very familiar with the assets and the intentions of the decedent. The surviving spouse is also the beneficiary of the residuary trust, while living, so they are normally only accounting to themselves.

Gathering Assets

Upon the death of the settlor of a revocable trust, the successor trustee of the trust must determine what assets are in the trust. Any assets not in the trust will not be under the control of the successor trustee. It must be determined what the proper legal title of the non-trust assets are and whether they need to go through probate. If the assets are sole name assets and have no designated beneficiary, the assets will need to go to probate. The successor trustee does not administer the probate estate unless he or she is appointed as the executor of the estate. The will of the deceased usually nominates an executor, but if none is nominated or the one nominated is unable or unwilling to act the court will appoint someone.

The job of the successor trustee can be difficult. It can be difficult to determine what assets an individual owned at the time of his or her death. If the successor trustee does not have previous knowledge of the decedent's financial affairs, the successor trustee must investigate to determine what the decedent owned. The investigation should begin by going through the decedent's mail, looking over tax returns, looking through safe deposit boxes, and speaking to the decedent's spouse (if one is living). This usually gives the successor trustee most of the information needed. Occasionally, mail will come in with other clues (normally year end financial statements for tax purposes).

The decedent can make the job of the successor trustee much easier by making a list of all the assets in the trust. The list of assets should describe the location of every asset in the trust, the approximate value of the assets, and the account number of any accounts or insurance policies. The successor trustee can use the list as a key to all the information received from other sources. The list will save the successor trustee hours of work that would be required to track down all of the trust assets. The list will also insure that assets do not slip between the cracks and get lost. There is no reason that a beneficiary should go without assets from the trust because they cannot be found.

Distribution

Before the successor trustee can think about distributing assets from the trust, the successor trustee must re-title the assets into the name of the trust, with the successor trustee as the new trustee, or into the name of the residuary trust, if one is created under the terms of the trust. All assets will be distributed from the re-titled trust.

The successor trustee must disperse the assets in the trust according to the terms of the trust. The assets cannot be distributed until the successor trustee is certain that the tax liability, if there is any, is accounted for and that all creditor's claims are satisfied.

All potential creditors of an estate should be notified during the administration of the estate. State laws require that this be done in specific time periods. The successor trustee must comply with the laws of the state in which the decedent was a resident. Once the creditors are notified, state law will dictate an amount of time in which they must respond or their claims will be barred. Valid claims must be paid by the successor trustee from the trust account. The trustee can challenge any claim that is invalid. However, any challenge to a creditor's claim will require legal fees and most likely a court proceeding. This could cost the estate additional funds to defend a lawsuit.

Once all creditor's claims are paid and all tax liabilities are paid, the successor trustee may make distributions to beneficiaries of the trust. The trustee must review the trust and any amendments carefully in order to determine which beneficiaries are to receive what assets. The trustee will make distributions of all specific bequests before residuary amounts are distributed. Once the specific requests are distributed, the trustee can then divide the assets between the residuary beneficiaries, if there are any. If there are no assets after the specific bequests have been paid, the residuary beneficiaries will receive nothing because the specific bequests get paid first.

Some assets are not distributed outright to beneficiaries and are held in trust. The trust may state that assets are held in any number of different kinds of trusts. Assets can be held in a residuary trust, a QTIP trust, or a spendthrift trust. All of these trusts involve the successor trustee continuing to act as trustee over a trust. The beneficiaries of these trusts will not receive assets outright and cannot do as they choose with the assets.

Releases

Before the trustee sends the beneficiary a check for the amount he or she is to receive from the trust, the trustee should send the beneficiary a release to be signed. The release should be an acknowledgment that the beneficiary has received the proper amount they are entitled to under the terms of the trust. The release should also waive any right the beneficiary has to make a claim against the trustee for the administration of the trust. This will ensure that the trustee will not be sued for his or her handling of the trust, or at least be evidence that the beneficiary accepted the devise and agreed to the way the trustee handled the trust.

All distributions to beneficiaries come from the trust account where the assets are held. If the asset is a piece of real property, the trustee must execute a trustee’s deed transferring title to the property to the beneficiary. Once the assets are distributed to beneficiaries, the beneficiaries own the assets and are free to do with them as they wish.

If Estate is Over the Unified Credit

If an individual passes away with over $1.5 million in his or her estate, the estate is subject to federal estate taxes. The estate is subject to federal estate taxes regardless of whether the assets from the estate are in a revocable trust. The revocable trust keeps the assets from being subject to probate. The only time the revocable trust helps to avoid federal estate taxes is when the trust is created by a married couple creating an AB trust. The AB trust maximizes the couple’s unified credit.

The successor trustee of the trust will be responsible for filing a Form 706 federal estate tax return if the estate is taxable. The Form 706 is due within nine months of the decedent’s date of death. At that time the successor trustee is responsible for any estate tax liability that is due. The successor trustee pays the tax liability from the assets in the estate. The successor trustee should not distribute assets until the tax liability is paid. Any tax liability that cannot be paid because the successor trustee has dispersed money is the responsibility of the successor trustee. The successor trustee can be held personally liable for the tax liability if there are no funds to satisfy it.

Post Mortem Planning

Very little can be done in respect to post-mortem, after the death of the decedent, planning. A few things can be done to lesson the tax burden on an estate. One such devise is called a disclaimer.

Disclaimer

A disclaimer is a mechanism used by estate planning attorneys to redirect assets upon the death of an individual. By executing a disclaimer as to portions of jointly owned assets, a beneficiary can effectively fund his or her spouse's credit shelter/residuary trust to its full $1.5 million capacity. This allows the assets to grow, estate tax free, without inclusion in the estate upon the beneficiary’s death, while still allowing the beneficiary to receive the income and any principal he or she may need for health, maintenance, and support. This will result in a substantial estate tax savings to the beneficiary’s heirs upon his or her death.

It is important that the beneficiary does not delay in deciding whether he or she wishes to proceed with the disclaimer as it usually must be executed within a certain amount of time. In addition, within the time period in which the beneficiary executes the disclaimer, the beneficiary may not receive a benefit from the assets he or she chooses to disclaim.

A disclaimer may be executed by any beneficiary who meets the above requirements. The only reason people usually choose to disclaim an asset is because they have over $1.5 million in assets and their estate is going to be subject to estate taxes. The legal fees an attorney charges to prepare a disclaimer usually dissuade an individual from using the disclaimer to pass assets to his or her children unless he or she will have a taxable estate. An individual can just gift the assets to his or her children once he or she inherits the assets.

Many people think that they can keep assets from creditors by disclaiming assets. However, an individual cannot disclaim assets when he or she is insolvent. This would allow individuals to avoid paying debts and runs against public policy. The disclaimer usually requires the individual to sign off to the fact that he or she is not insolvent.

Chapter 17
Conclusion

Intelligently Discuss Issues With Clients

The goal of any professional should be to discuss estate planning issues intelligently with their clients who are attempting to or have done their estate planning. While it is not the role of a financial planner or insurance agent to advise people on legal issues, it is important that these professionals can discuss estate planning with clients to understand client's goals.

A client's goals in financial planning and purchasing insurance products are integrally tied to his or her estate plan. Understanding estate planning issues and being able to discuss them is a vital tool for professionals dealing with individuals planning their futures.

See Potential Problems With Estate Planning

It is just as important for a financial planner or insurance agent to see potential problems with an estate plan as it is to give good advice. Business professionals can save their clients a great deal of heartache and some money by spotting problems in their estate plans. Clients are often misinformed or misunderstand the probate process and the federal estate tax.

A business professional can build a great deal of trust with a client by providing some good advice about his or her estate plan. What better way to provide good advice than to tell a client that his or her estate plan is flawed and how to correct it?

In the event that the issue is too complicated for the business professional, he or she should have a reliable attorney to consult. Sometimes you do not need to know the answer, you just need to know that something is wrong and be able to lead the client to someone who knows the correct answer.