HOW TO PLAN YOUR ESTATE TODAY

By

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“And Joseph made it a law over the land of Egypt unto this day, that Pharoah should have the fifth part.”

-Genesis 47:26

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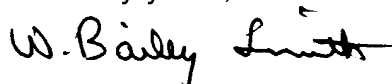
Dear Friends and Clients:

When I was selected by a major trust institution to address the attorneys of Los Angeles County, Orange County, and San Diego County, the title of my talk was "The John Wayne Problem and the Bing Crosby Solution." This speech discussed the importance of the revocable living trust as a way to avoid probate and save death taxes. Although written for attorneys, I believe you will appreciate the enclosed copy.

I will meet with prospective clients on a courtesy basis. If you would like me to review your current will (and / or trust), please bring it along with a financial statement, your spouse (if married), and copies of the grant deeds and property tax bills to any real estate you may own. My main office is in Newport Beach at the above address. I also have a branch office in Long Beach at the California Bank and Trust Company, 444 West Ocean Blvd., Suite 900 (corner of Magnolia and Ocean Blvd.).

I'll be delighted to meet with you at no cost nor obligation.

Sincerely yours,



W. BAILEY SMITH

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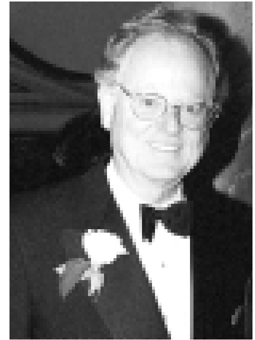
I. THE JOHN WAYNE PROBLEM AND THE BING CROSBY SOLUTION©



By W. BAILEY SMITH

Estate planners owe a duty to their clients. This duty is not just to create an estate plan for the clients, but also to explain it to them in such a way that they can easily understand it.[1] Therefore, this article will explore:

1. Verbal explanations to lay persons of estate planning concepts and terms; and
2. Written handouts (see pages 16 - 42) that may be given to clients after the initial interview, that will aid the client in understanding estate planning.[2]

The public has not acted on revocable living trusts because the legal profession has not done an adequate job of simplifying this complex area into a format that is understandable. Obviously, if attorneys continue to use Latin words and confusing tax terms when they explain the advantages and the disadvantages of the trust, they will lose their clients. There is too much technical literature and not enough information on client communication.

My approach is simple and basic so that the client understands what we are trying to do. A recent survey conducted by my office of 800 homes in a nearby community (where the average home value is $500,000) showed only one half of the homes were held by the owners as trustees of their own trust. Less than 50% of the individuals in this survey had funded revocable living trusts.[3] We are not getting our message across to the general public.

The following story of two famous Californians and how they

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planned their estate is useful in educating the public, as the public shows an interest in the lives of famous people. Bing Crosby planned his estate the smart way by achieving privacy, avoiding unnecessary delays, saving fees, avoiding a conservatorship, and saving time. John Wayne planned his estate in an inefficient way.

The choices that confronted these famous Californians, Bing Crosby and John Wayne, are the same choices that confront us and our clients. Do you want to plan your estate the smart way, the efficient way, by saving time, achieving privacy, and avoiding unnecessary expenses; or do you want to plan it the inefficient way?

The idea of the revocable living trust has been around for a long time. In fact, if the year were 1808 rather than 2008, and if you were planning your estate, you would be thinking about this exact same idea. Even back in medieval England the idea of the trust was a very flexible one that allowed individuals to avoid some harsh laws (such as the law of primogeniture – which was the exclusive right of the eldest son to inherit his father's estate).

The trust concept is one that applies not just to the rich like the Rockefellers, the Vanderbilts, the Buffets, the Gates, and the Du Ponts. It is just as appropriate now for the middle class because of the inflationary spiral of values and the confiscatory nature of death taxes and statutory probate fees.

What Is a Revocable Living Trust?

It's a simple idea and can be easily understood if we break it down to its lowest common denominator. A trust is nothing more than a contract. If you are married, it would be a contract between you and your spouse establishing a manager for your assets, stating how your assets would be handled while you were both alive, and what would happen to those assets at the death of one or both of you. For example, John Doe and Mary Doe transfer their assets to "John Doe and Mary Doe, Trustees

of the Doe Family Trust" for the benefit of John Doe and Mary Doe during their lifetime and then to their children equally. It can be individually tailored to suit your own family needs.

These trusts are just as effective for single people as they are for married couples.

A "living" trust is one that is established while you are alive, wherein you would actually transfer assets from your individual names to your names as trustees of your own trust. For example, John Doe and Mary Doe would transfer title to their house from "John Doe and Mary Doe as joint tenants" to "John Doe and Mary Doe, Trustees of the Doe Family Trust."

Living trusts are established during life for individuals who wish to avoid probate. Testamentary trusts are established at death; they spring out of your last will and testament. Testamentary trusts go through probate. Both testamentary and living trusts can save death taxes, but the living trust has an added advantage over the testamentary trust in that it also avoids the agony and expense of probate.

The living trust is also "revocable". This means that you can change your mind at any time regarding the assets transferred into the trust, the assets removed from the trust, the trustee(s) of the trust, and the beneficiaries of the trust. In essence, you are the "captain" of your own ship setting its course. You can amend any portion of the trust at any time or revoke the entire trust.

Revocable living trusts are sometimes known by other names. You may have heard of this concept as the "inter vivos trust." "Inter vivos" in Latin means "among the living". Sometimes the revocable living trusts are called "grantor trusts," "AB trusts," "ABC trusts", "marital deduction trusts," or "probate avoidance trusts".[4]

Why Consider A Revocable Living Trust?

This leads us to the John Wayne problem. John Wayne did not choose to have a revocable living trust. Therefore, his $12,788,865.06 estate became a public record.[5] The exact nature of his assets, to whom they passed, whom he loved within his family and whom he didn't, are reviewable as a public record at the County Courthouse. He did not achieve privacy. John Wayne's probate took over six years.[6] The statutory probate fees for the attorney and the executor for John Wayne's estate were in excess of $275,000, which could have been avoided.

Privacy

Bing Crosby had been through a similar situation when his first wife, Dixie Lee Crosby, died in the 1950's. He did not have enough cash to pay the death tax after her death. So he had to sacrifice a number of his assets in order to raise cash. In addition, Bing Crosby was very upset by the publicity generated by Dixie Lee's death. Publicity about her estate was obviously publicity about his estate because of the community property nature of California law.

When Bing Crosby later planned his own estate he wanted to be sure he achieved privacy. He did not want anyone to know the size of the estate, or where it was going. When he died, there was no publicity about the size of his estate, whom he left it to, or where his assets were going, because he had a "private will." [7] Bing Crosby had established a revocable living trust. Therefore, privacy is one reason you should consider a living trust.[8]

Avoiding Probate

Another reason to consider a living trust is to avoid the delay of probate. A decedent usually has title in his name to various assets, such as stock certificates, grant deeds, passbook accounts, etc. Removal of the decedent's name from these various certificates of title so that the surviving family members

can deal with them is the process of probate. This title clearing process in a small estate in the State of California generally takes about a year and one-half. However, these time delays can be avoided by transferring the assets into a living trust. Rather than spending years transferring assets to surviving family members, it can be settled within a matter of months.

Another advantage of a living trust is avoiding the cost of probate. Probate fees are set by statute and are based on the gross value of the decedent's estate. Suppose the decedent had a home, car, stocks and some cash in the bank. If this all added up to a gross estate of $300,000, and if he had a mortgage against that house of $100,000, then his net estate would be $200,000. Taxes are based on the net estate. However, probate fees are based on the gross estate ($300,000) and cost approximately 4%-8%. Therefore, in this example, probate fees would be about $18,000. Yet, this $18,000 expense could be completely avoided by transferring assets into a living trust before death.

Avoiding Guardianships

A living trust allows you to avoid the problems of a guardianship. A minor who inherits property cannot deal with that property because of his tender age.[9] The State of California will step in through a guardianship proceeding, take control of those assets, and transfer those assets to an adult to manage for the benefit of the minor. The guardian of the estate of the minor is required to post bond, which is an expense the estate must pay on an annual basis. The guardian must give periodic accountings back to the Court and explain how the money is being spent for the benefit of the minor. These periodic accountings are expensive because they are prepared by accountants, and presented to the Court by attorneys on a regular basis. In addition, these guardianship proceedings are public. The worst part, however, about the guardianship proceeding is the fact that at the age of 18, the minor gets the assets free of any further control. What do you think an 18-year-old would do with

$200,000 in assets? Most 18-year-olds are not mature enough to handle large sums of money.

A better way to handle property going to a minor is to pass it to that minor in trust, wherein you, not the state, decide who will be the trustee and the manager of the assets for the benefit of that minor. You can waive the bonding fees, you can waive periodic accountings, you can make the money available to the minor for his college education, or for any medical needs or support, without giving the minor control of the money until he is more mature. You determine at what age he will get the money. For example, you can say that after you and your spouse have passed on, that your estate will continue in trust for the benefit of your minor child. Your minor child may have the right to use the money for his support and education, but he may not have the money for a sports car or sailboat until he is 30, 40, or whatever age you select.

Avoiding the Groucho Marx Problem

A living trust can avoid the Groucho Marx problem. Groucho Marx got caught in a conservatorship because he became senile. Conservatorships, like guardianships, are proceedings whereby the State of California steps in through its court system and takes control of the individual's assets because that individual is not able to manage his own assets. These conservatorship hearings are not just for the aged, but also for those who have premature heart attacks, strokes, dementia, and other health problems that prevent them from managing their own estate.

These incompetency hearings are usually embarrassing for the entire family. A court investigator will be called into the case to talk to the elderly individual, the family is in court to testify, and a judge must make a decision as to whether or not that individual is competent to manage his own affairs. If that individual is not competent, then the court will

appoint an individual to manage his affairs for him. A court appointed manager must post a bond. Bonds are expensive and paid for out of the estate. A court appointed manager must make accountings to the court as to how the money is being spent for the benefit of the incompetent. These reports are done on a regular basis, prepared by accountants and presented by attorneys. They are expensive. Like guardianships and probates, these conservatorships are also public. Your friends, your neighbors, and your family can discover the details of your financial portfolio.

Why not avoid the potential Groucho Marx problem by establishing a living trust stating that when and if you get to that point in your life where you can no longer manage your own affairs, then you want your spouse or good friend, John Doe, to manage them for you?

Avoiding Out Of State Probates

A living trust can also avoid a probate in other states. For instance, if you own a condominium in Hawaii and a farm in Iowa when you die, you will have a probate not only on your California assets, but you will also have a probate on the real estate you own out of state. You will have a triple probate, because the farm in Iowa and the condominium in Hawaii will also be going through a separate probate. Why not avoid the triple probate by setting up a living trust in California and transferring not only your California real estate into that trust, but also all of your non-California real estate?

Avoiding Family Battles Over Your Plan

If you think somebody may contest your estate plan, a living trust makes sense. A will is relatively easy to contest; whereas a living trust is more difficult to overturn.

A Type Of Premarital Agreement

A living trust can act as a type of premarital agreement in that it will segregate and keep separate property separate.

Save Taxes

A living trust can also save taxes. For instance, if both spouses die in 2008, the federal estate tax on a $2,500,000 estate would be $230,000 under the typical all-to-spouse type will. However, with a revocable living trust, this tax could be completely eliminated and your family would save $230,000 in taxes. The actual tax savings depends on the size of the estate, the year of the death, and the type of estate plan established.

These tax savings are in addition to any probate savings. For example, in a $2,500,000 estate, you could save about $230,000 in taxes, in addition to the probate savings of approximately $76,000. The combined savings could be $230,000 in taxes and $76,000 in probate savings, for a total of $306,000. This means a couple could transfer $306,000 more to their children rather than losing it in unnecessary taxes, costs and fees.[10]

Avoid the Gigolo and The Floozy

Have you taken advantage of the “anti-gigolo” and the “anti-floozy” trust? This is an arrangement whereby you can pass your entire estate on to your surviving spouse to maximize the tax advantages and yet ensure that at your surviving spouse’s later death, your share of the estate will come back to your children and not go out to a new spouse or other romantic interest of your surviving spouse.

FEDERAL DEATH TAXES IF BOTH SPOUSES DIE IN 2008

Estate Size	Taxes on a Trust	Taxes on a Simple Will	Tax Savings with Trust
$1,500,000	$0	$0	$0
$2,000,000	$0	$0	$0
$2,500,000	$0	$230,000	$230,000
$3,000,000	$0	$460,000	$460,000
$4,000,000	$0	$920,000	$920,000

Be Your Own Trustee

Who should the trustee be? Most of my clients choose to be their own trustees. If something should happen to one spouse, then the surviving spouse takes over. If the surviving spouse needs help, then an adult child, a trust company, or bank can step in as the successor trustee.

What Assets Belong to Your Trust?

To take full advantage of the probate avoidance opportunity that the living trust offers, you should transfer all of your major assets into the trust. However, there are three assets that are normally not put in: 1) one checking account, 2) your cars, and 3) your qualified plans (like IRAs, 401(k)s, Keoghs, Pension and Profit sharing plans).

Conclusion

In conclusion, we all have a choice of how we plan our estate. We can plan it the smart way, avoiding probate, achieving privacy, saving time, eliminating death taxes, avoiding the Groucho Marx problem, and avoiding guardianships, or we can plan it the inefficient way. The choices that John Wayne and Bing Crosby made are the same choices with which we will all be confronted. What have you decided?

FOOTNOTES

1. We all have a duty to our clients to eliminate the legalese and the technical terminology in favor of plain English. See Kellogg, Managing an Estate Planning Practice, 3rd edition, California Continuing Education of the Bar, (1982)

2. Why re-invent the wheel? Most clients have the same questions about the living trust. After presenting the documents to the client and answering their questions, why not give them a memorandum of frequently asked questions that they can keep with their original documentation? (See page 25.) This is a great reference for the client because it answers 99% of all their questions about the documents that have been prepared on their behalf. It saves your office time as it eliminates answering their questions a year or even years after the documents have been established and explained to them. The memorandum can also reduce the likelihood and magnitude of malpractice claims. Desmaris, "Legal Malpractice in Estate Planning and Administration and How to Avoid It," ESTATE PLANNING, TRUST AND PROBATE NEWS, State Bar of California, Winter/Spring 1983, Vol. 5, No. 5, p. 14.

3. This Survey would seem to substantiate Dacey's claim that: "I would put the proportion of lawyers who are both willing and competent to set up an inter vivos trust as well under 10%." Dacey, How to Avoid Probate, (fifth edition, 1993), p. 46.

4. We learn about 10% through hearing, but about 80% through sight. Visual aids are extremely important in making your clients feel comfortable with this new trust concept. Give them an example. Show your clients a copy of a previously written trust and point out the highlights. Then, give them a visual example of how easy it is to establish a trust. For example, hand $100 to the wife. Tell her that she is going to help you set up a trust so they will have a better idea of what a trust is, and how simple it is to establish. Advise her to invest the cash for the benefit of her husband. Instruct her to pay the interest that she earns each year to her husband, and if he is in need of any additional funds for his support, health, education and maintenance, she is authorized to invade the principal for his benefit. This is a "revocable" arrangement (since all trusts are revocable in California unless expressly stated to be otherwise). Obviously, this is a "living trust" because it's being set up during life. The creator can change her mind about the beneficiary, or the assets being transferred. Next, tell her that you have had a change of heart and now wish to revoke the trust. Thereupon, take the $100 back. This is a simple visual illustration of how the concept works.

5. John Wayne is not the only Hollywood star who left a public record. Henry Fonda's $4,139,986 estate, and Natalie Wood's $5,939,925 estate make for some interesting readings as well. Both are located at the Los Angeles County Courthouse, Hall of Records.

6. Petition For Preliminary Distribution filed November 23, 1983, in the Probate Department of the Orange County Superior Court. John Wayne, also known as Marion Michael Morrison, died testate on June 11, 1979, in Los Angeles County as a resident of Orange County. His October 5, 1978, will was admitted to probate on July 10, 1979 and took six years in court to administer and a guardianship continued under court supervision after John Wayne's probate was closed.

7. Bing Crosby's attorney, Richard S. Arnold, Los Angeles Times, October 15, 1977, page 3.

8. The hallmark of the Revocable Living Trust for the last 800 years has been privacy. However, the California Legislature (and only the California Legislature) has decided to require that the Trust become a quasi-public record at the Trustor's death; and therefore notice of the Trust's existence and its terms must now be given within 60 days of the Trustor's death to all beneficiaries and heirs for all decedent's dying after January 1, 1998.

9. Amounts of $5,000 or over are subject to a guardianship. California Probate Code §3400 and §3402.

10. Another visual example that helps clients understand this trust concept is to explain it to them with a box. In the past, I have used chalkboards, graphs, and cut-up paper. Now I use a clear, plastic box that I hand to my clients, telling them that this represents their trust. If they want to avoid probate, avoid conservatorship, avoid publicity and guardianships, save time and money, then they will establish a trust which is represented by the box in their hands.

A trust is simply a container for assets. To take full advantage of the trust, they will want to transfer their assets into the trust. I begin with the transfer of their home. It will be transferred into their trust by changing title on their grant deed from the two of them as individuals to the two of them as trustees of their own family trust. I then put a model home into the plastic box. There is no increase in property taxes because there is an exception under Proposition 13.

Next, we talk about transferring their savings accounts. I hand them passbook savings accounts. I tell them the title to these accounts will be changed from the two of them to the two of them as trustees of their own trust. By making this change on the title to their passbook accounts, their savings accounts will move into the trust. I then place the passbooks into the box so they can visually conceptualize what we are talking about.

Next, we transfer title on their stock certificates to the two of them as trustees of their own trust. I then put stock certificates into the plastic box.

Finally, I have a string that I connect to the box and then to the two clients to emphasize the revocability of this agreement. They can change their minds at any time about the terms or the beneficiaries in this trust. They can also change their minds about any of the assets in the trust simply by pulling on that string and taking the asset out.

11. If “a lawyer should always act in a manner consistent with the best interest of his client,” then a day is coming (if it is not already here) when it will be malpractice not to discuss the option of avoiding the agony of probate via the revocable living trust. Thode, The Ethical Standard for the Advocate, 39 Texas Laws Review, 575, 592, (1961) American Bar Association Cannons Ethical Consideration 7-9.

12. Richard M. Kettley, The Estate Planner’s Notebook, Kettley Publishing Company, Newport Beach, California, page E2.

13. Ibid, Page E191.

14. In addition to the references to Kettley’s masterpiece and Kellogg’s excellent summary, see Turner’s Revocable Trusts, Fourth Edition, 2001 (West Group) and Weinstock’s Planning an Estate, Fourth Edition, 2002 (Shepard’s McGraw & Hill). One of the best books for the lay person is Who Gets It When You Go?, by David C. Larson, Revised 1997.

II. HOW DO YOU HOLD TITLE TO YOUR INVESTMENTS?

Most people hold title to their investments in joint tenancy, but this is often not the best way to hold title. To determine how you hold title to your investments look at your title documentation. If you hold title in joint tenancy it will read "John Doe and Mary Doe, as Joint Tenants" or "John Doe and Mary Doe, Husband and Wife, with the Right of Survivorship." This means the property automatically passes to and becomes owned by the surviving joint tenant upon the death of the other joint tenant.

The reason joint tenancy is such a popular method of holding title to your investments is that it is a simple way to take title and it avoids probate at the death of the first joint tenant. (Probate means court supervision of your estate at your death. Probate is expensive and takes time, so most people like to avoid it whenever they can.) People think they are saving time and money by taking title to their investments in joint tenancy. However, there are some real problems with joint tenancy.

1. Joint Tenancy Does Not Always Avoid Probate

First, joint tenancy does not avoid probate upon the death of the last owner. For instance, if you and your spouse own your investments as joint tenants and you die, the investment passes to your spouse free of probate. However, when your spouse dies, unless she has placed your investment in joint tenancy with others, the property will be probated because there is not a surviving joint tenant. The same is true of bank accounts, stocks and other assets you have placed in joint tenancy. If, on the other hand, these investments were placed in a living trust, you could arrange it so there would be no probate on your death nor on the death of your spouse. Joint tenancy only postpones probate, it does not avoid probate.

2. Your Will Does Not Act On Joint Tenancy Assets

A second problem with joint tenancy is that a joint tenant's will does not control where the property goes. For example, you may intend to leave everything to your wife, but if you have a joint checking account with your son, then upon your death your son, not your wife, will get the checking account. If your son then gives your checking account to your wife, he will be making a gift and he may have to pay a federal gift tax.

3. Joint Tenancy Often Causes Assets to Disappear

A third problem with joint tenancy is that the property can end up in the hands of beneficiaries to whom you did not intend to leave it. For example, take the investment that went to your spouse. Suppose your spouse remarried and, wanting to avoid probate, makes her new spouse a joint tenant in the ownership of the investments. If she dies, her new spouse gets the investments and your children receive nothing. This is probably not what either of you had intended.

Another variety of this type of problem is the childless couple. Assume that one spouse dies. All of the joint tenancy property goes to the surviving spouse and later if she dies without a will, the property goes 100% to her family. In other words, all of the property goes to the relatives of the last spouse to die, thereby cutting out the relatives of the spouse who died first.

4. Joint Tenancy Can Result in Gift Tax Liability

The fourth problem with joint tenancy is a potential federal gift tax problem. For example, if you put $50,000 of I.B.M. stock in joint tenancy with your son, then you are obviously making a gift. Anytime you make a gift of more than $12,000 per year per individual, you have a possible gift tax liability.

5. Joint Tenancy Is A Death Tax Trap

The fifth problem with joint tenancy occurs when one wants to avoid unnecessary death taxes. Holding assets in joint tenancy causes those assets to pass to the surviving joint tenant rather than into the tax savings trust. By holding title to assets in joint tenancy, you are often incurring unnecessary death taxes.

6. Joint Tenancy is An Income Tax Disaster

The biggest problem with joint tenancy is the income tax problem. This is best illustrated by the following: Suppose you bought stock in 1990 for $50,000 and today it is worth $250,000. If you sold this stock while you and your spouse were both alive, the difference between your cost ($50,000) and your sale price ($250,000) would be $200,000. This $200,000 would be subject to tax at long-term capital gains rates. However, if you held onto that stock until the death of one of you, the tax would depend on how you held title. If you held title as joint tenants, then $100,000 would be subject to long-term capital gains tax because only the decedent's one-half of the stock would get a stepped-up basis to the fair market value at death. If you held title as community property, then nothing would be subject to capital gains tax, because both halves would get a stepped-up basis to the fair market value at the date of death.

It is important to remember that holding title to appreciated assets as community property, not joint tenancy, will result in a lower income and capital gains tax. You can still avoid probate by putting these assets into your living trust and you can avoid the income tax disaster of joint tenancy by taking title to those assets in community property. In short, you can have your cake and eat it too, if you use the living trust.

In summary, joint tenancy is a death tax trap and an income tax disaster. Joint tenancy should be avoided in most estates.

STATUTORY PROBATE FEES

The State of California has established the “minimum” cost of probate which is set forth in the chart below. However, it is most unusual to complete the probate process at such a low fee because the chart does not include extraordinary fees granted by the court for sales of assets during probate, preparation of death tax returns (Form 706), litigation expenses, etc.

Probate Assets	Probate Fees	Probate Assets	Probate Fees
$10,000	$800	$675,000	$33,000
20,000	1,600	700,000	34,000
40,000	3,200	725,000	35,000
60,000	4,800	750,000	36,000
80,000	6,400	775,000	37,000
100,000	8,000	800,000	38,000
120,000	9,200	825,000	39,000
140,000	10,400	850,000	40,000
160,000	11,600	875,000	41,000
180,000	12,800	900,000	42,000
200,000	14,000	925,000	43,000
225,000	15,000	950,000	44,000
250,000	16,000	975,000	45,000
275,000	17,000	1,000,000	46,000
300,000	18,000	1,100,000	48,000
325,000	19,000	1,200,000	50,000
350,000	20,000	1,300,000	52,000
375,000	21,000	1,400,000	54,000
400,000	22,000	1,500,000	56,000
425,000	23,000	1,600,000	58,000
450,000	24,000	1,700,000	60,000
475,000	25,000	1,800,000	62,000
500,000	26,000	1,900,000	64,000
525,000	27,000	2,000,000	66,000
550,000	28,000	2,500,000	76,000
575,000	29,000	3,000,000	86,000
600,000	30,000	3,500,000	96,000
625,000	31,000	4,000,000	106,000
650,000	32,000	5,000,000	126,000

*In excess of $5,000,000 add 2% of the excess to $126,000

"Probate Assets" means assets actually passing through probate administration. Fees are based on the gross value of each asset plus income receipts, plus gains on sales, less losses on sales, during probate administration. This chart represents the total statutory fee for both the attorney and the executor.

1. WAYS TO AVOID PROBATE

A. Joint tenancy

B. Life insurance

C. Retirement plan benefits

D. Revocable trusts

E. Irrevocable trusts

F. Totten trusts

G. Private annuities

H. Property passing to a spouse

I. Uniform Transfers to Minors Act

J. Gifts

Joint tenancy is simple to use and is fine for the smaller estates, however, it can create a real death tax trap and income tax disaster in the larger estates because it will prevent the death tax savings provided by a trust from working at the death of the first joint tenant, and because only the decedent's one-half gets a stepped-up value in basis for federal income tax purposes.

"Totten" trusts are taxed to the creator during his lifetime and also at his death. For example, "John Doe, trustee for the benefit of John Doe, Jr." It's good for the small estate to avoid probate or for an estate consisting entirely of cash. However, these "pay on death" accounts are not true trusts. Totten trusts do not avoid taxes, do not avoid conservatorships, and often do not avoid probate.

2. PROBATE

A. DISADVANTAGES:

1. Cost
2. Time
3. Complexity of the probate system
4. Publicity
5. Accounting
6. Confusion

B. ADVANTAGES:

1. Protection of the heirs, creditors, and tax entities.
2. Termination of all creditors claims after four months.

THE REVOCABLE LIVING TRUST COMPARED TO THE TESTAMENTARY TRUST

THE REVOCABLE LIVING TRUST
(Created During Your Lifetime)

Advantages
1. No probate.
2. No conservatorship.
3. Privacy.
4. Avoids delays in distributing assets.
5. Tax deductible.
6. Acts as a pre-nuptial agreement.

Disadvantages
1. More expensive to establish.
2. Care in transferring assets into the trust.

VS.

THE TESTAMENTARY TRUST
(Created After Your Death)

Advantages
1. Less expensive to establish.
2. Simpler.

Disadvantages
1. Subject to probate.
2. Subject to conservatorship.
3. Public record.
4. Periodic accounting.
5. Delay in distribution of assets.

THE REVOCABLE LIVING TRUST
A GRAPHIC ILLUSTRATION

John Doe's Will:

All assets that I own at my death pass into the Doe Family Trust.

Jane Doe's Will:

All assets that I own at my death pass into the Doe Family Trust.

DOE FAMILY REVOCABLE LIVING TRUST

Creators:	John and Jane Doe
Managers:	John and Jane Doe
Property:	All real and personal property
Control:	100%
Revocable:	100%
Amendable:	100%
Primary Beneficiaries:	John and Jane Doe
Secondary Beneficiaries:	Children of John and Jane Doe

WHAT TYPE OF ESTATE PLAN IS BEST FOR YOU?

TYPE OF PLAN	Taxes Saved?	Probate Avoided?	Guardianship Avoided?	Conserva-torship Avoided?	Fee is Tax Deductible?*
1. **Intestate:** No Plan; No Will	No	No	No	No	No
2. **Holographic Will:** "Do-it-yourself Special"	No	No	No	No	No
3. **Simple, All-To Your-Spouse Will:** "Mom and Pop" Will	No	No	No	No	No
4. **Testamentary Trust**	Yes	No	No	No	Yes
5. **Simple, Revocable Living Trust:** Probate avoidance only	No	Yes	Yes	Yes	Yes
6. **Standard, Revocable Living Trust:** Probate avoidance and tax savings	Yes	Yes	Yes	Yes	Yes
7. **Legacy (Dynasty) Trust** Probate avoidance and tax savings for three (3) generations	Yes	Yes	Yes	Yes	Yes

***The Tax Reform Act of 1986 provides that tax advice is deductible to the extent it exceeds 2% of your adjusted gross income.**

III. FREQUENTLY ASKED QUESTIONS ABOUT THE LIVING TRUST

1) What Is A Revocable Living Trust?

A trust is a contract whereby one person transfers property to another person for the benefit of a third person. For example, “A” transfers property to “B” to manage for the benefit of “C.” If the creator of this arrangement sets it up during his lifetime, it is called a “living trust.” If the creator retains the right to dissolve this trust, it is a “revocable” living trust.

A living trust also avoids probate. This is the most widely advertised advantage of a living trust. Although this represents a substantial savings, it must be compared with the expense of establishing the trust.

The revocable living trust avoids publicity. Estates which pass through probate are a public record. Not only is the will available to all who want to see it, but also an inventory of the decedent’s assets. You can easily avoid this publicity and achieve privacy by transferring assets into a living trust. Property in the trust will be kept private, both as to its nature, and as to who receives it.

A trust avoids the “Groucho Marx” problem. A trust can avoid the embarrassment and the publicity surrounding an incompetency hearing if you place all of your assets into the trust prior to the time that you become legally incompetent. Rather than have the court determine whether or not your are incompetent, you can decide who will make that determination. For example, a family doctor, a close friend, your golf buddies, or your children could make that decision.

2) Does A Bank Or Trust Company Have To Be Involved?

No, the law does not require a corporate trustee even though your individual circumstances may suggest this is a good idea. If an individual or a husband and wife are willing and able to assume the responsibilities of being their own trustee, they can do so. When an individual’s death, incapacity or lack of desire necessitates it, a successor trustee steps in. The successor trustee may be anyone you

choose to nominate, i.e., a good friend, a child over the age of 18, your minister, or a professional such as a trust company or a bank.

3) If I Set Up a Trust, Is A Will Also Required?

Yes. A will is always drafted in conjunction with your trust. The will acts as a safety net. If you forgot to transfer all of your assets into the trust, then the will would pick those assets up at the time of your death and transfer them into your trust whereupon the assets would be distributed pursuant to the terms of your trust. This "pour-over will" makes sure that any assets that were not transferred into the trust during your lifetime will pour over into the trust at your death. If all of your assets have been transferred into the trust during your lifetime, the pour-over will may never be used and it never has to be admitted into probate.

4) Why Is It Important To Transfer Assets Into The Trust?

To avoid the agony of probate. Those assets in the trust will avoid probate, save time and money, and achieve privacy. Assets not registered in the name of the trust will cause a probate. The way you transfer assets into the trust is by changing title from you individually to you as trustee of your trust. It is not sufficient to just list assets on the schedule attached to the trust. You must actually re-title your assets into the name of the trust in order to avoid probate.

5) Must I Transfer All Of My Assets Into My Trust?

No, but to avoid probate you would want to transfer all of your major assets into the trust. Only those assets in the trust will avoid probate. Four assets are normally not transferred into the trust because they pass free of probate: 1) Automobiles, 2) IRA's (and other types of qualified retirement plans), 3) One checking account in joint tenancy, 4) Annuities.

6) Is It Necessary To Put Personal Property Into The Trust?

No. If your personal property is of nominal value, then it can be transferred free of probate. There is no need to transfer it into your trust. However, if you have valuable antiques, coins, stamps, etc., then these assets should be registered in the name of the trust.

7) Will Property Taxes Be Increased By The Transfer Of My Real Estate Into My Trust?

No, there is a special exemption under Proposition 13. There is no increase in property taxes by transferring your real estate into the trust.

8) Revocable or Irrevocable?

A living trust may be either revocable or irrevocable. Revocable means you can cancel or alter its terms. Irrevocable means it is set in concrete and you cannot change it.

9) Can A Living Trust Save Death Taxes?

Yes. A living trust can save substantial amounts in death taxes. For example, if you and your spouse die in 2008 with an estate of $2,500,000, a living trust can save you $230,000 in death taxes. The death tax is also known as the estate tax or the inheritance tax. The death tax is an unfair tax because it is a tax imposed on assets that you have already paid income tax on. The death tax is also a confiscatory tax because the death tax rate can be as high as 45% of your estate.

10) Do I Need A Special Tax I.D. Number For My Trust?

No. If you alone, or you and your spouse together, are acting as trustees of your trust, then the only identification number that will be required for your trust will be your social security number. No special identification number is required. The special number is referred to as the SS-4 number, the 95 number, or the tax I.D. number of the trust.

11) Must Special Income Tax Returns Be Filed?

No fiduciary income tax returns (541’s or 1041’s) are required as long as you and your spouse, or you alone, are acting as the trustees of your trust.

12) Why Doesn’t Everyone Have A Trust?

Most people do not know about living trusts. Many people do not take the time to plan for their future. Many people do not like to discuss death nor to plan for it. Most attorneys know nothing about living trusts.

13) Does A Living Trust Make Sense For A Single Person?

Yes, these trusts are just as effective for single people as they are for married couples – regardless of whether or not a person is a widow, widower, spinster, or bachelor.

14) Does A Trust Make Sense For Someone Who Has An Estate Of Less Than $1,000,000?

Yes, because that person can still avoid the agony of probate. Anyone who has $200,000 in assets or more should have a trust because a $200,000 estate would cost $14,000 to probate. The larger the estate, the larger the savings. Trusts can be set up for individuals who have any size estate – even for people with modest estates.

15) Are Legal Fees Establishing A Trust Tax Deductible?

It depends on the type of trust you establish. If you establish a tax-savings trust, then 80% - 90% of the fees are tax deductible under I.R.C. Section 212.

16) Is The Living Trust A New Idea?

No, it has existed for hundreds of years.

17) The Living Trust Is Sometimes Known By Other Names:

“THE A-B TRUST” OR “ABC TRUST”
“THE MARITAL DEDUCTION” OR “THE QTIP TRUST”
“THE GRANTOR’S TRUST”
“THE MARITAL & RESIDUARY TRUST”
“THE BYPASS TRUST”
“THE INTER VIVOS TRUST” (“Inter vivos” in Latin means living)

18) There Are Many Different Types Of Trusts

The living trust should not be confused with:

“Off-Shore Trusts” – These are trusts set up for the creditor protection for individuals who have large estates requiring sophisticated liability planning.

“Testamentary Trusts” – These are trusts that come out of your last will and testament and go through probate.

"Totten Trusts" – This is not a true trust, but rather a way to take title to your bank account so as to avoid probate at death, e.g., "A" as Trustee for "B." These are also called "pay on death" accounts.

19) I Already Have A Living Trust.

If you already have a living trust, ask yourself these questions:

1. Has it been updated to take advantage of the current law? All trusts should be reviewed at least every five years.

2. Have you funded your trust? (i.e., Have you re-registered all of your assets to your names as trustees of your trust?)

3. Have you coordinated the way you hold title with your trust so that assets will pass into the trust?

4. Why not get a second opinion of your old trust from an attorney who specializes in trusts?

20) Why Didn't My Attorney Tell Me About The Living Trust?

Many attorneys are not knowledgeable about the living trust because they do not specialize in estate planning. It's also possible your attorney was told you only wanted a will, or everything in joint tenancy with your spouse, or the least expensive estate plan. If you had asked your attorney to recommend the best estate plan for you, the living trust would have been mentioned.

21) Does The Living Trust Restrict My Rights To Borrow On My Assets In The Trust?

No. Although lenders may want to see a copy of the trust, the trust does not restrict your rights to borrow on assets in the trust in any way. Some lenders may prefer to lend on real property outside of a trust and ask you to transfer that real property out and then secure the loan. Always make sure that you or the lender transfer your real property back to your trust.

22) Does This Protect Me Against My Creditors?

No, the living trust does not act as a barrier to creditors for the creators of the trust because the trust is revocable. However, at the death of the creators of the trust, the "spend-thrift" clause can

act as a legal barrier for funds that continue to be held in the trust for the benefit of the children.

23) What Rights Does The Surviving Spouse Have In The Trust Assets?

If the surviving spouse is the surviving trustee, he or she has the right to buy and sell and transfer any of the assets. The surviving spouse is usually the beneficiary of the trust assets and, therefore, has the right to all the income and to invade the principal. The surviving spouse has the freedom to do whatever he or she wants with the assets in the trust.

24) Does My Will Avoid Probate?

No. Your will does not avoid probate. All the assets passing through the will pass through probate. Probate is a title-clearing process. Probate is expensive, time-consuming, and public. Most people want to avoid it. You can avoid probate with a living trust.

25) Who Are The Parties To The Trust?

1. The creator of the trust is referred to as the "trustor."

2. The manager of the trust is referred to as the "trustee."

3. The "beneficiary" or "beneficiaries" of the trust is/are the person or persons for whom the trust is established.

All three hats can be worn by the same person or by the same couple; you and your spouse can both be the creators, the managers, and the beneficiaries of your own trust. If you are single, you alone could be the creator, the manager, and the beneficiary of your own trust.

26) What Are Constitutional Trusts?

Constitutional trusts are sometimes known as "Patrick Henry" trusts, "Common Law" trusts, "Family Equity" trusts, or "Pure Equity" trusts. These types of arrangements should be avoided because the I.R.S. has attacked them as a sham and will disallow deductions and assignments of income. These trusts are illegal tax protests and will incur a negligence penalty if established. They are an attempt to eliminate income, estate, and gift taxes. The labor of the taxpayer

along with his assets, home, and business, are transferred to a "trust" and the taxpayer receives shares back from the trust. Usually the taxpayer is the creator of the trust, the manager of the trust assets, and also the beneficiary. Constitutional trusts are a disaster and should be avoided.

27) Does A Living Trust Avoid Probate On Out-Of-State Realty?

Yes. You can avoid probate on out-of-state realty by transferring those properties into your California trust. For example, if you own land in Arizona and a condominium in New York, you can avoid probate in Arizona and New York by transferring those out-of-state assets into your California Trust.

28) Does A Living Trust Protect me From Someone Contesting My Estate Plan?

Yes, a living trust can give you better protection than a will from somebody attempting to contest your estate plan. If you feel someone may attempt to contest your estate plan, you would be better protected with a trust.

29) What Will You Charge Me For A Living Trust?

That depends on how much time is required and how difficult the job is. Each client has different objectives, family circumstances, and assets going into the trust. I will give you a set fee immediately if I can predict in advance what will be involved. Otherwise, I will give you an estimated minimum and maximum fee. Generally fees range between $2,500 to $5,000 depending upon the complexity of the trust and the surrounding documentation.

30) Do I Need A Lawyer To Establish My Trust Or Can I Do It Myself?

You can attempt to prepare your own trust without an attorney but the results will likely be worse than if you had done nothing. For example, Chief Justice of the U.S. Supreme Court, Warren Burger, prepared his own will and messed it up. Burger chose not to consult an estate planning attorney and the decision cost his family about $457,000 of his $1,800,000 estate because of unnecessary taxes and court costs.

31) A Husband's Most Valuable Gift

This is what the Reader's Digest recently called the living trust because it can bring comfort and peace of mind to the wife who may eventually become a widow.

IV. FREQUENTLY ASKED QUESTIONS ABOUT POWERS OF ATTORNEY

A power of attorney is a written contract given by a principal to an agent to perform specified acts on behalf of the principal. It acts as a delegation of authority.

The person who holds a power of attorney is called an "attorney-in-fact" or "agent". He is empowered to act in the place of the principal as to all acts necessary and proper for the transaction of business that is within the scope of the authority granted under the power of attorney.

1) Attorney-In-Fact Distinguished From Attorney At Law

A power of attorney does not permit the attorney-in-fact to act as an attorney at law. An attorney-in-fact differs from an attorney at law by definition. The State Bar Act restricts the practice of law in California to active members of the State Bar.

2) Persons Capable Of Granting Power Of Attorney

Any person having the capacity to contract may appoint an agent. All persons with the exception of minors, persons of unsound mind, and persons deprived of civil rights, are capable of contracting and may grant a power of attorney. Minors are expressly precluded from granting powers of attorney.

3) Persons Capable of Acting As Attorneys-In-Fact

Any person may be an agent. As a practical matter, however, only persons capable of contracting can act effectively under a power of attorney.

4) Authority of Attorneys-In-Fact In General

A principal may authorize an attorney-in-fact to do any acts

that the principal might do. An attorney-in-fact has the actual authority that the principal confers upon him.

An attorney-in-fact has authority to do everything necessary and proper in the ordinary course of business to effect the purpose of the power of attorney.

5) General Vs. Special Power Of Attorney

A general power of attorney gives the attorney-in-fact full authority to transact any and all kinds of business for the principal. A power of attorney is a general power unless it is specifically limited by the principal. A special power of attorney limits power only to those items especially set forth in the document.

6) What Is A Springing Power Of Attorney?

Ordinarily, a power of attorney is effective as of the day it is signed and executed. This means that even if you are competent to make your own decisions, your attorney-in-fact will also have the legal authority to act on your behalf and engage in financial transactions. A “springing power of attorney,” on the other hand, becomes effective at a later date, usually when the principal becomes mentally incompetent. It “springs” into effect at the point you lose capacity, as certified by your physician.

7) If I Have A Living Trust Do I Still Need A Power Of Attorney For Asset Management?

Yes, because there are some decisions that have to be made on your behalf which do not come within the powers of the trustee.

8) If I Have A Living Trust Do I Still Need A Power Of Attorney For Health Care?

Yes. A trustee under a living trust does not have the authority to make medical decisions on your behalf. A trustee can use trust assets to pay for medical care, but they cannot make medical decisions.

9) Advance Health Care Directives

This form is to be used when a principal wishes to confer upon another person the power to make health care decisions for the principal. It is legally enforceable but “Living Wills” and “Directives to Physicians” are not. It allows you to die with dignity. It allows you to get off life support. You don’t have to die as a

vegetable. In exercising authority under an advance health care directive, the attorney-in-fact has a duty to act consistently with the principal's desires.

10) Duration Of Advance Health Care Directives

When did you sign your advance health care directive? Any advance health care directive signed before January 1, 1992 has expired.

11) Revocation Of Advance Health Care Directives

At any time while the principal has the capacity to execute an advance health care directive, he may revoke the appointment of the attorney-in-fact by notifying the attorney-in-fact orally or in writing.

12) Effect Of Acts Of Attorney-In-Fact

All acts of the attorney-in-fact performed under a durable power of attorney during a period of the principal's incapacity have the same effect, and inure to the benefit of and bind the principal and his successors in interest, as if the principal were competent.

13) Lock Up On Medical Records

In 2003 a new law to protect patients' medical records and health information took effect. Because of this law (HIPAA) we now suggest that you update your durable power of attorney for health care forms. Many medical providers are refusing to release medical information to the agent specified in the durable power of attorney if the new HIPAA language is not there.

We encourage you to contact our office to have a new durable power of attorney document for health care prepared.

14) Termination Of Powers Of Attorney

A power of attorney is terminated by the occurrence of any of the following as to every person who has notice:

1) The revocation of the power by the principal;

2) The expiration of its term;

3) The death of the principal;

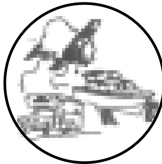
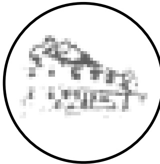
4) The death of the attorney-in-fact;

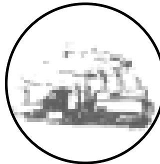
5) The renunciation of the power by the attorney-in-fact; or

6) The incapacity of the attorney-in-fact to act in that capacity.

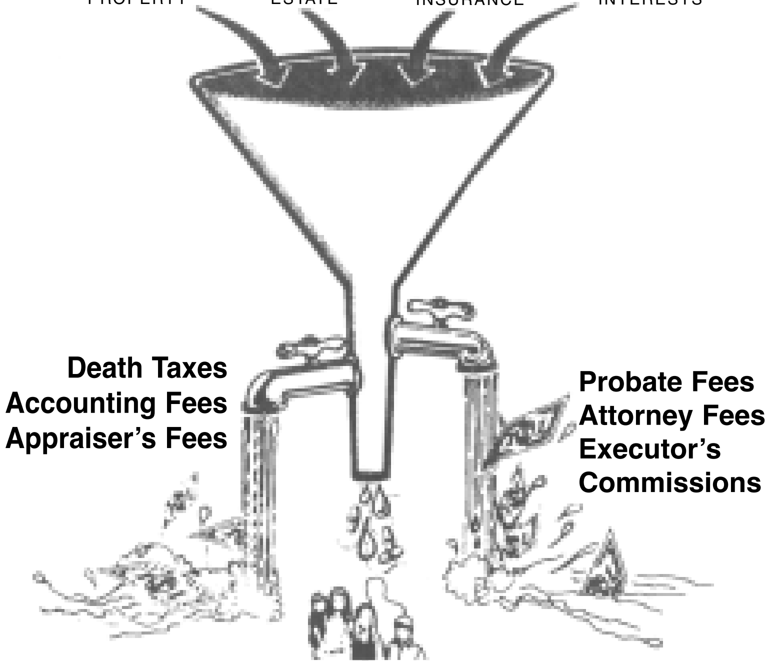
WHAT HAPPENS TO YOUR ESTATE AT DEATH?

It passes through the estate settlement cost funnel



PERSONAL PROPERTY
REAL ESTATE
LIFE INSURANCE
BUSINESS INTERESTS



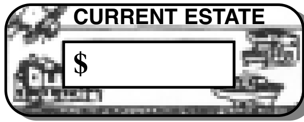
Death Taxes
Accounting Fees
Appraiser's Fees

Probate Fees
Attorney Fees
Executor's Commissions

Proper estate planning will get more to your family

Footnote No. 12

THE A-B-C TYPE TRUST ARRANGEMENT



DEATH OF FIRST SPOUSE

	TRUST A	TRUST B	TRUST C
	SURVIVOR'S TRUST	**EXEMPTION TRUST** (Unified Credit Trust)	**Q-TIP TRUST (Qualified Terminable Interest Property)**
Assets Allocated To Each Trust	**ESTATE ASSETS** • Survivor's Separate Property • Survivor's Half of Any Community Property • Property Received from Decedent's Estate, If Any $	**ESTATE ASSETS** Only enough of the decedent's estate to exhaust his or her Applicable Exclusion of $2,000,000. $	**ESTATE ASSETS** Any portion of the decedent's separate or community property not allocated to Exemption Trust. $
Typical Provisions	**SURVIVOR RECEIVES:** • All Income • Full Power To Withdraw Principal • Unlimited Power to Dispose of Remainder at Death.	**SURVIVOR RECEIVES:** • All income (or sprinke income among surviving spouse and children) • Power to Use Principal for Survivor's Health, Support, Education and Maintenance. • Limited Power in Survivor to Appoint Remainder Unequally Among Children • Unlimited Power to Withdraw the Larger of $5,000 or 5% of Trust Principal Annually for Any Purpose.	**SURVIVOR RECEIVES:** • All income • Any Distribution of Principal During Surviving Spouse's Lifetime. **ADVANTAGE OF Q-TIP** First spouse to die can determine who will get his or her estate after the demise of the surviving spouse.
Federal Estate Tax Treatment	**DECENDENT'S DEATH** - NO TAX - Unlimited Marital Deduction eliminates the tax. **SURVIVOR'S DEATH** - FULLY TAXABLE - (On assets in excess of $2,000,000)	**DECENDENT'S DEATH** - NO TAX - Decedent's Applicable Exclusion avoids the tax. **SURVIVOR'S DEATH** - NO TAX - Survivor's interests in the trust are not taxable.	**DECENDENT'S DEATH** No tax, if executor elects to qualify trust for the Marital Deduction, otherwise it is taxable. **SURVIVOR'S DEATH** • Fully taxable if not taxed at decedent's death. • Not taxable if taxed at decedent's death.

CHILDREN'S TRUST OR
OTHER FINANCIAL BENEFICIARIES

Footnote No. 13

V. ADVANCED ESTATE PLANNING TOPICS

Although your living trust provides the foundation for your estate plan, it is often necessary to address more advanced estate planning topics as well to accomplish additional goals you may have for your estate. These may include such areas as the best manner to avoid divorce, to avoid creditors, to avoid taxes on your life insurance, to pass your IRA or other retirement plans to your children, to provide funds for your children's educational needs, and using available tools to reduce (or eliminate) death taxes.

Eliminating The Confiscatory Death Tax

Anyone with a net worth over $2 million should be aware that the death tax (also known as the estate tax or inheritance tax) continues to impose a substantial burden which could result in the loss of 45% of the estate in 2008 & 55% of the estate in 2011. However, the good news is that for those who properly plan their estate, this confiscatory death tax can easily be avoided simply by making use of legal loopholes provided by Congress, as discussed below.

1. Legacy (Dynasty) Trusts

Most people leave their estate outright to their children after their children have reached the ages of 30, 35, or 40. However, if you want to protect your children from creditors, divorce, lawsuits, and future death taxes at their own deaths, you should consider leaving their inheritance to them in an ongoing trust also known as a Legacy (Dynasty) Trust. The children could be the Trustee of their respective trusts. Your children could spend the income and principal if they wanted but their inheritance would be protected from lawsuits, creditors, divorce, and pass death tax free to your grandchildren.

2. Irrevocable Life Insurance Trusts

Life insurance passes income tax free but not death tax free. If you have a $1,000,000 life insurance policy it will pass income tax free to your children but your estate will pay about $500,000 in death tax. You can avoid this confiscatory $500,000 death tax

by moving your life insurance into an Irrevocable Life Insurance Trust. With an Irrevocable Life Insurance Trust your children would receive the $1,000,000 free of both income tax and death tax.

3. Qualified Personal Residence Trust (QPRT)

Congress has provided a way to reduce the death tax on your home using a special type of trust known as a Qualified Personal Residence Trust (QPRT), which allows you to transfer your residence to your children at a significantly reduced gift tax cost and with no death tax.

The QPRT is established when you transfer your residence to the Trustee of the QPRT, who will allow you to continue to use the residence for a fixed number of years specified in the trust instrument (the ‘fixed term’), which should be a term you are likely to survive.

During the fixed term, you will continue to pay mortgage expenses, real estate taxes, insurance, and expenses for maintenance and repairs, and will continue to deduct mortgage interest and real estate taxes on your individual income tax return. When the fixed term ends, the residence is distributed to your children, or remains in further trust for them.

Even after the fixed term ends, you can continue to use the residence by reacquiring or renting it from your children, or having the residence retained in trust for your spouse’s lifetime, thus assuring that the residence is available to you.

Although your transfer of the residence to the QPRT is a taxable gift, it is usually structured to result in a gift amount less than the gift tax exemption, so no tax is due. In addition, during the fixed term you will continue to have the power to sell the residence if you choose to do so and take advantage of the capital gains exclusion generally available for personal residences.

4. Charitable Remainder Trust (CRT)

A Charitable Remainder Trust (CRT) is a special trust which allows you to make a gift to the charity of your choice, which they will receive at some point in the future, or after your demise. Until

then, you will receive from the CRT an annual payment you specify, and an immediate income tax deduction. In addition, the CRT is exempt from income taxes, so these types of trusts are commonly used to sell appreciated property.

For example, if you sold $50,000 worth of stock that you bought years ago for $10,000, you would pay a capital gains tax of $6,000 on the $40,000 of gain, plus the state income tax, which would leave you with net sales proceeds of less than $44,000. However, if instead you contributed the stock to the CRT, it can now sell the stock and pay zero capital gains tax, because the CRT is exempt from income tax. Therefore, the CRT now has $50,000 to invest, instead of the $44,000 you would be left with. The CRT can then invest this additional $6,000 to generate a higher income stream for you for the rest of your life.

As an additional benefit, you are allowed an income tax charitable deduction for the year you create the CRT.

5. Family Limited Partnerships (FLPs) and Limited Liability Companies (LLCs)

The FLP and LLC are entities you may form to hold your investment assets which will allow you to transfer non-controlling entity interests to your children or other beneficiaries. Among the many benefits of the FLPs and LLCs are the following:

-You keep control of the underlying property
-You choose the amount and timing of income distributions to owners
-Valuation discounts allow you to reduce your death and gift taxes
-FLP and LLC assets are protected from attack by creditors of the owners
-Personal assets of the owners (you and your family) are protected from attack by the creditors of the FLP or LLC

Although FLPs and LLCs are very useful and effective planning tools for assets such as securities, investment real estate, and active business operations, they are not good devices for assets such as retirement plan accounts and personal residences.

6. How to Beat the IRS by Using Legal Loopholes

In a recent meeting with the chief estate and gift tax collector for the IRS western region, he stated, "The death tax in America is a voluntary tax. The only people who pay it are those who don't properly plan their estate!" Many estate plans include legal loopholes designed to take advantage of tax saving opportunities provided by law. However, it is imperative to follow the formalities required by the plan.

For example, your living trust is just one type of loophole. The trust may provide that upon the death of the first spouse, the trust assets are to be divided between the deceased spouse's share and the surviving spouse's share. This division is intended to avoid having the deceased spouse's share unnecessarily subject to estate tax upon the subsequent death of the surviving spouse. If instead this division is not implemented and appropriately documented at the time of the first spouse's death then the trust structure is ignored by the IRS resulting in additional estate tax.

Similarly, the necessary steps must also be followed in the administration of more advanced loopholes, such as Qualified Personal Residence Trusts, Generation Skipping Trusts, Self Cancelling Installment Notes (SCINs), Grantor Retained Annuity Trusts (GRATs), Irrevocable life Insurance Trusts, Family Limited Partnerships (FLPs) and Limited Liability Companies (LLCs). These obligations include tasks such as keeping financial accounts in the name of the entity to prevent commingling with personal assets, and doing likewise with income and expenses. Further, entities such as FLPs & LLCs must also comply with specific state and federal reporting requirements.

If you do not respect the form of your estate plan, neither will the IRS, and the tax savings and other benefits otherwise available through your planning will be lost.

Naming the Beneficiary of your IRA Account-Stretch IRA

Individual Retirement Accounts (IRAs) play an important role in your retirement strategy. You have an opportunity to turn your traditional IRA into an effective estate planning tool by making appropriate IRA beneficiary designations. For example, "stretching" the tax deferred growth of IRA assets (potentially over several generations) can assure assets pass efficiently to your children and grandchildren.

By rolling over assets to an IRA, an account owner has the ability to use beneficiary designations to reduce required minimum distributions for both the account owner and beneficiaries, and therefor lowering annual taxes and extending the life of the IRA.

What is a "stretch" IRA? When an account owner names a beneficiary younger than himself this is sometimes referred as a stretch IRA. When this younger beneficiary receives the inherited IRA, the remaining balance is paid out over the younger person's life expectancy, effectively stretching out the length of time that withdrawals can be taken out from IRA. This extends the period of tax-deferred earnings of assets within an IRA beyond the lifetime of the person who set up the IRA.

Who should be the beneficiary of the IRA? As a very general rule, it is probably best to name your spouse as the primary beneficiary, your adult children as secondary beneficiary, and the Successor Trustee of your Revocable Trust as a third choice.

The custodian of your IRA has the beneficiary designation forms that you need to fill out. You should contact the custodian directly and request copies of those forms to review them in light of your option to take advantage of this new rule.

Planning for your IRA, 401(k), and Other Retirement Plans

Because an IRA, 401(k), or other pension or retirement plan is often a significant part of your total estate, it is necessary for these accounts to be appropriately addressed when planning your estate.

The maximum estate and income tax deferral is usually achieved by naming your surviving spouse as the designated Primary Beneficiary. You may also choose to designate as a Secondary or Contingent Beneficiary your children or other heirs, or your living trust, depending on your facts and circumstances.

Educational Needs Planning

Both 529 Plans and Coverdell Savings Accounts allow you to invest money on a tax deferred basis. That means that any investment earnings are not subject to current income or capital gains taxes. In addition, these earnings are also exempt from income tax when withdrawn if they are used for qualified higher education expenses for the beneficiary of your choice.

529 Plans are usually the most attractive of these two choices because contributions can reach up to $250,000 for each beneficiary's account and are not limited by the income of the donor, compared to the Coverdell Savings Account which limits contributions to $2,000 per year, or less for families with a six figure income.

The 529 Plan gives you more control over the account funds, including changing beneficiaries, deciding the timing and amount of distributions to the beneficiary of your choice, and making investment decisions.

In addition, while both 529 Plans and Coverdell Savings Accounts are not included in your estate for death tax purposes, this benefit is more valuable for 529 Plans because the balances may be higher, and your contributions may be "front loaded" to take advantage of 5 years worth of the $12,000 annual exclusion from gift tax.

When shopping for a 529 plan, you should consider costs, investments options and asset-allocation strategies.

1. Weigh any **tax advantages** of investing an in-state plan against the plan's total costs.
2. Look for annual **asset-based fees** of less than 1% for direct-sold plans and less than about 1.3% for broker-sold plans.
3. **Compare state plans** at www.savingforcollege.com www.collogesavings.org or www.morningstar.com.
4. For information on California's 529 plan visit www.scholarshare.com or call (877) 728-4338, toll free.

MISCELLANEOUS

Periodically review your estate plan to make sure it is up to date. A regular review of your estate plan is important not only as far as complying with new laws, but also to ensure that you have named the right fiduciaries and that the plan for distribution of your estate continues to meet your current objectives. The older you are and the greater your financial wealth, the more frequent your periodic review should be (for example, every three (3) years). Everyone's estate should be reviewed at least every five (5) years.

An Aggregate Property Agreement between you and your spouse may be necessary to maximize the death tax savings made possible by your living trust fully utilizing both spouses' estate tax exemption amount.

WARNING: You can only avoid probate for those items that are placed into your trust. It is your duty to check title to all of your assets on a regular basis to ensure that they are in the trust in order to avoid probate.

These materials have been prepared by W. Bailey Smith for reference and educational purposes only and may not reflect the most current legal developments. There is no assurance that the material provided is correct or in compliance with federal, state or local laws or practices in any respect, or suitable for any purpose for which you intend to use it. This author is not acting as a lawyer for you or anyone else. Do not use the forms contained in this booklet without the advice and supervision of a lawyer admitted to practice law in the relevant jurisdiction.

VI. WHAT HAPPENS AFTER DEATH?

1. Order at least twelve (12) certified copies of the Certificate of Death through the funeral home. A certified copy of the Certificate of Death will be needed for each insurance policy, IRA, 401(k), and each additional asset (real estate, stocks, bonds & mutual funds) that you will transfer or sell. The Certificate of Death must be a certified copy obtained from the County Recorder's office. As soon as possible, meet with your trust attorney to have him review the details of the trust so you understand your obligations and benefits. Your attorney will need: (a) a current financial statement listing all of the decedent's assets and liabilities as of the date of death, (b) the decedent's original will and any original codicils and, (c) at least two certified copies of the decedent's Certificate of Death.

2. If there will not be a formal probate proceeding, your attorney will file for safekeeping the decedent's original will with the clerk of the superior court in the county of the decedent's residence. The law requires that you file the original will for safekeeping within thirty days of the date of death.

3. The decedent's qualified plan (ie. IRA, 401(k), pension & profit sharing plans) should be rolled over by the surviving spouse into their own IRA within 60 days to avoid income taxes.

4. Real estate is reassessed at death. You must file a Preliminary Change Of Ownership Report in all counties where the decedent owned real estate to avoid any increase in property taxes. Failure to file the Preliminary Change Of Ownership Report with the County Assessor may result in a reassessment of the property tax.

5. If the decedent had a trust and any portion of that trust became irrevocable at the decedent's death, then you must promptly give notice to the decedent's heirs and beneficiaries advising them of the terms of the trust and that they are entitled to a copy of the decedent's trust.

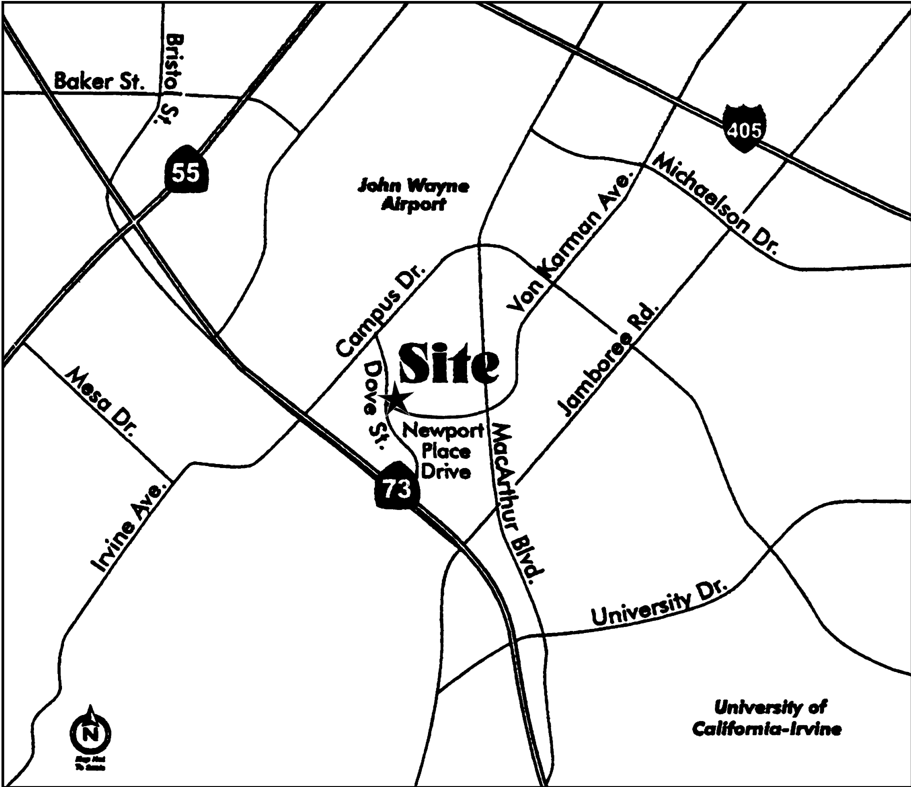
6. Your attorney will want to review a list of all of the assets and liabilities as of the date of death to determine whether or not a Federal Estate Tax Return, “Form 706”, will be required. If the gross estate of the decedent is $2,000,000 or more, the Form 706 is required and must be filed by you under penalty of perjury within nine months of the decedent’s date of death.

7. Fiduciary income tax returns may be required if any of the trusts become irrevocable at the death of the first spouse. Fiduciary income tax returns may also be required after the death of the second spouse if the trust administration is not completed quickly. Your attorney will obtain the taxpayer identification numbers for the irrevocable trusts for you from the Internal Revenue Service.

8. Do not ignore the terms of the trust, otherwise, the Internal Revenue Service may deny you the tax benefits which were one of the main reasons you established the trust in the first place.

9. DO NOT make changes to the ownership of any assets, including bank account registrations, until you have met with your trust attorney, otherwise valuable estate planning opportunities (e.g., disclaimers) may be lost.

10. Update your will, trust, and durable powers of attorney for both health care decisions and property.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BUSINESS IS GOOD *AND* WE'RE LOOKING FOR MORE!

The continued success of our firm depends on the quality of our service. Our continued growth depends on new clients. We are accepting new business and appreciate your referrals.

NOTES

Miscellaneous Quotes on Taxes

"The death tax in America is a voluntary tax. The only people who pay it, are those who don't properly plan their estate!"

-Chief Tax Collector, IRS

"What is the difference between a taxidermist and a tax collector? The taxidermist takes only your skin."

-Mark Twain

"The Family Limited Partnership and the Limited Liability Company wrappers allow one to take assets and reduce their value by 30%."

-The Chief Tax Collector for the IRS in Southern California

"If Patrick Henry thought that taxation without representation was bad, he should see how bad it is with representation.

-The Old Farmer's Almanac

"There is no art which one government sooner learns from another than that of draining money from the pockets of the people."

-Adam Smith

"A shroud has no pockets."

-Anonymous

"We don't pay taxes. Only little people pay taxes."

-Leona Helmsley

"Anyone may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase ones taxes."

-Judge Learned Hand

"…nothing in this world is certain but death and taxes."

-Benjamin Franklin, 1789

"The art of taxation consists in so plucking the goose to obtain the largest amount of feathers with the least possible amount of hissing."

-Jean-Baptist Colbert

"The hardest thing in the world to understand is the income tax."

-Albert Einstein

"The Federal Estate Tax Return (Form 706) is an invasive, complex and ridiculous return."

-The Chief Tax Collector for the IRS in Southern California

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