

# It's Frankly Not That Interesting

December 2010 from James M. Kane, Attorney

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Observing what motivates people to respond to situations, or their failure to respond, is a very interesting aspect of my work as a lawyer. This is true regardless of whether one is involved in planning matters, transactional work, or litigation. We all suffer from shortcomings in various facets of our motivations (yes, even lawyers).

As to estate planning, and not to be glib, it is helpful candidly and simply for me to acknowledge to clients that estate planning is frankly not that interesting.

By contrast, estate planning is inescapably important and can touch on a complex combination of tax, property, probate, and trust issues that need to be considered in the planning stage. This is the case particularly in many higher net-worth situations

The estate planning process also, in my view, is much more realistic if clients understand it is widely typical that most people are simply not energetically motivated to sit down, take the necessary time, and complete whatever is needed to get his or her estate planning in place.

Thus, estate planning has to be viewed like taking medicine. That is, take a breath, stop for a moment, and just push through the inertia, resistance, and hesitation. The pain and problems are often much less if one will simply stop and take the medicine.

This newsletter provides a framework of

information a client can use to begin taking the medicine, and push through to the finish line for his or her estate planning.

As a beginning framework, the following is a brief description of the combination of estate planning documents many clients put into place for their core estate planning:

(1) A written Declaration of Trust (one trust document separately for each spouse). This is their core estate planning document. It includes all necessary trust provisions that apply during the client's lifetime, also during the surviving spouse's lifetime, and for the client's children and their descendants (and, if desired, the spouses of the descendants).

(2) A related pour-over Last Will and Testament. This Will essentially moves, at the time of the client's death, the client's property into his or her Declaration of Trust (to the extent not already in the name of the Declaration of Trust when the client was alive). The Declaration of Trust thereafter is the controlling estate planning document.

(3) A financial power of attorney.

(4) A health care directive (essentially, a health care power of attorney).

Now, here are some fundamental points that will help clients understand what their estate planning documents are helping achieve:

**The EP Documents Become You** – Many people believe that an estate planning document merely states who is to get the estate property. So, then why not simply write this on the back of an envelope or a short piece of paper? The reality is that most situations are not that simple.

Ponder, for a moment, what would happen if your death or incapacity were to occur right now. Upon death or incapacity, your estate planning documents (or the absence or shortcomings in your documents) become you, your virtual *alter ego*.

Who you were (while alive) is now subject to your documents, or lack thereof. Every single financial, investment, and business matter you handled prior to your death or incapacity is now governed by your documents (or lack thereof). The ongoing care for your family centers on these documents.

Thus, estate planning documents are often complex as a preventive measure due to the virtually unlimited circumstances they may have to address, particularly otherwise to avoid the need to seek direction and oversight by the courts in the absence of having addressed these in your estate planning.

**Deferral of Estate Tax** -- The estate tax law allows a married couple to defer estate tax until the death of the surviving spouse, regardless of the size of the estates. The estate tax is then applicable based on the value of the estate at the surviving spouse's death. A couple's estate planning documents need to include this deferral mechanism.

Keep in mind this deferral of estate tax for a married couple is allowable only if the first spouse's estate property passes either outright to the surviving spouse or in a trust for the surviving spouse (with the surviving spouse being the sole beneficiary for his or her lifetime).

**Estate Tax on FMV of Your Property** -- The federal estate tax is computed on the FMV of

your property at the time of death (or the FMV when the surviving spouse dies for the above deferral), less the estate exemption amount allowable under the tax law. The estate tax generally applies to all property you own at the time of your death, including life insurance, annuities, and other retirement assets (pension plan, IRA, 401(k), etc.). Some states also have an estate tax (in addition to the federal estate tax).

**A QTIP Marital Trust** -- I typically recommend a "QTIP Marital Trust" mechanism for the deferral of estate tax for a married couple. This is a trust that holds property for the surviving spouse funded with the first-to-die spouse's estate property. The term QTIP is from the tax law and means "qualified terminable interest property."

The written terms of the QTIP Marital Trust are within your core Declaration of Trust. These written QTIP provisions direct how liberal you wish for the trust provisions to be for the benefit of your surviving spouse.

In many cases a married couple will want the QTIP trust to be as liberal as possible so that it virtually replicates the surviving spouse having unrestricted access to the trust, but still preserves the benefits of using the trust.

But, in some marriages with children from a previous marriage, and so forth, the first-to-die spouse may wish to include more restrictive access to the QTIP trust by the surviving spouse.

A key question for you to consider is who will be the trustee of the QTIP trust for the surviving spouse. In many cases the surviving spouse can be the sole trustee.

**Benefit of Using Trusts** – The essence of trusts is that you can set up controls and limitations for the trust property, compared merely to the beneficiaries getting the property outright.

Trusts (compared to outright ownership) also provide (i) a considerable amount of asset protection for the beneficiaries of your estate,

and (ii) will give your estate much greater flexibility for certain post-death tax planning and related options that can provide after-death tax planning and related tax savings, when compared to your property merely passing outright to your beneficiaries.

Using trusts (with the provisions written in your Declaration of Trust) is also my recommendation for how your property will be held and administered for your children after both your deaths. Each child, as part of the design of your Declaration of Trust document (if you prefer), can be the sole trustee of his or her own trust share.

**Selecting the Names for Your Executor & Trustees** -- This is one of the most important considerations for your estate planning documents. That is, who will be the executor of your estate, and who will be the trustee of the above trusts for your surviving spouse and ultimately for your children.

**Guardians for your Children** -- Finally, for clients with children under age 18, the most difficult question is the naming of the guardians for minor-aged children in the unlikely event both parents die.

**A Possible Second Stage of Estate Planning** -- In some instances after a client completes the above core estate planning documents, there

may be a need for looking at a second stage of planning. This second stage, if necessary, involves more specific asset protection, and estate and gift tax planning. It deals with various aspects of additional planning with joint-property agreements, gifting and life insurance trusts, gift planning, GRATS (grantor retained annuity trusts), sales of property to certain trusts (often called grantor trusts), inter vivos QTIP trusts, techniques for the fragmentation and discounting of property, state versus federal estate tax planning, generation-skipping transfer tax (GST) planning, and more-focused asset protection, just to name a few.

To the extent, and whether, you need to implement the second stage of planning will take into account a balancing of the time and expense of the additional planning compared to the benefits (e.g., asset protection, tax savings).

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