Get it Done this Year (2012)

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I start this newsletter with one uncertainty and one certainty.

The uncertainty is whether many of us (yes, including me) will this year review and put our estate planning in order, or will we put it off for another year.

The certainty is that we will at some point die, and prior to death possibly have a period of incapacity.

Many of us believe we ultimately will one day *feel like taking on* the task of our estate planning. My experience, however, is that expecting this feeling is illusive and most of us will continue feeling like not taking on this task. Realistically, the key is simply to push through with the necessary effort and get it done, and behind you. This year 2012.

This newsletter is intended to help you move this estate planning process to the finish line.

Your Documents Become You

Your estate planning documents become your *alter ego* when you die or later become incapacitated.

For example, if your death (or incapacity) were to occur on a Tuesday. Beginning on Wednesday, all financial, property, tax, legal, business, etc., matters that you would have handled personally will now be handled according to the directive and instructions in your documents.

And, if your documents are non-existent, incomplete, or include gaps that do not cover certain circumstance, your family likely will have to respond to the gap by seeking costly court oversight to remedy the problem. This requires lawyers.

Core Estate Planning Documents

Core estate planning documents for each spouse consist typically of a pour-over Last Will and Testament with a companion revocable living trust (called a "Declaration of Trust"), and financial powers of attorney and health care proxies.

The specific design of these core estate planning documents depends on my review and analysis of your particular situation. The revocable trust approach is better for most clients, in my opinion, particularly if a spouse later becomes incapacitated.

A second level of estate planning may apply for more extensive estate or gift tax planning, etc. We can discuss whether your situation might warrant this additional level of planning. Some clients do not need additional planning.

Asset–Protection Considerations

My general view of estate planning is that if you are going to invest time and money in the estate planning process, your documents need also to dovetail and include asset protection features, to the fullest extent possible.

For some clients who face even greater exposure for asset-protection purposes (due to their occupational risks, etc.), the above core estate planning might also include what is called an "inter-vivos QTIP trust". This is a particular type of trust a married couple can implement, and fund now, with their property.

Two primary reasons for this inter-vivos QTIP

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trust are: (i) this QTIP trust presently provides an excellent level of trust asset protection for the trust property not available if the spouses otherwise own their property outright; and (ii) the property in the QTIP trust will be available to absorb the estate tax exemption amount for whichever spouse is the first-to-die, as well as the exemption for the second-to-die, regardless of the ordering of the spouses' deaths. Thus, the QTIP trust helps best ensure use of both spouses' exemptions.

Back to core estate planning. The following key points are important for any course of action you take for your estate planning:

No Estate Tax Until After Both Your Deaths

The estate tax laws for federal and state purposes are generally designed so that a married couple does not pay estate tax (if any tax is payable) until after both spouses have died. This is the case regardless of the size of the couple's estates. Your core documents can be designed to take into account this second-to-die spouse feature.

Thus, generally at the surviving spouse's death is when the day of reckoning occurs for determining whether any estate tax will be payable.

Trusts for Your Beneficiaries

For the core documents I recommend, your beneficiaries will not get property from you outright at your death. Instead, your estate planning documents will include trust provisions for your beneficiaries (e.g., subtrusts for your children and whichever one of you is the surviving spouse) rather than having your property pass outright to them. Your children will not become beneficiaries until after both your deaths.

You and your family members can be trustees if you prefer. This is quite typical.

In some situations clients can include a 90-day withdrawal option to give each child a choice of either taking the property outright or leaving it in the trust set-up. This option applies only after both parents' deaths.
All of the trust instructions, etc., will be written as part of your core estate planning documents.

No new trust documents will have to be prepared at your death.

I most frequently prefer trusts rather than outright distributions of the property. Trusts provide (i) the ability of your successor trustee to oversee and manage the property; (ii) much greater asset protection of the property from third party claims, lawsuits, etc.; and (iii) a much broader array of tax options, particularly in response to future changes in circumstances or the law.

Trusts Help You Mandate Limitations

If your beneficiaries get property ultimately from you outright, they end up having absolute control over the property. They can give it to anyone, including a new spouse, someone else's children, friends, etc. Complete *carte blanche*. They also can lose it in a divorce or bankruptcy much easier if not in trust.

By contrast, the written terms of your trusts, for example, will mandate that your property is available (after your death) only for whichever one of you is the surviving spouse and thereafter only for your children and their descendants.

This greatly helps protect the property from second marriages, divorce, children from someone else's marriage, etc.

As to this protection, a very compelling illustration of this mandate was presented in a recent estate planning Atlanta seminar. These are examples from this seminar about the practical benefit of trusts:[1]

> ***Example 1***: Donna, having inherited $750,000 from her parent's estate, carefully places the inherited funds in a [financial institution] investment account. Donna has the account titled in her name as her "sole and separate property," to segregate the assets from her

and her husband Steve's other assets. Donna and Steve have been married five years, their marriage is solid, and they have a young child. Steve has decided start a business, and has negotiated a $575,000 loan from First State Bank. Steve tells Donna that the bank won't make the loan unless Donna co-signs the note (or, perhaps, unless the loan is secured by Donna's [financial institution] investment account), and Steve asks her to co-sign.

Example 2: Same facts as in Ex. 1, except that the $750,000 that Donna inherited was left in a trust of which Donna is the trustee. The trust contains a spendthrift clause. Again, Donna co-signs Steve's note. She is personally liable on the obligations, but the trust assets cannot be reached because of the spendthrift clause.

Example 3: Same facts as in Ex. 2, except that Steve, instead of attempting to borrow money from the bank, asks Donna, as trustee, to either (i) loan the funds to Steve or (ii) invest trust funds in his business. Here, Donna has no choice but to point out that, in view of her fiduciary duties as a trustee, (i) a loan to a relative would constitute impermissible self-dealing, and (ii) investing trust funds in a start-up company would be an imprudent investment not within the "prudent investor' standard.

Provisions for Your Children's Spouses

I do not typically include your children's spouses as beneficiaries. But there will be written provisions in the documents that allow whichever one of you as the surviving spouse to carve out benefits from the trusts for a child's spouse, if you so choose.

Each of your children (after both your deaths) also will have the power under the terms of your core documents to carve out benefits for their spouses, if they so choose.

Executor and Trustee; Your Choice

Without my going into the functional distinction in this letter between an executor and trustee, you will designate in your estate planning documents these positions. You will also name successors in the event an executor or trustee is unable to serve.

Your named executor and trustee will have the responsibility for managing your property and affairs after your death or incapacity and will carry out the trust terms and instructions for your *alter ego* as mandated in your core estate planning documents. In other words, the executor and trustee (can be the same person) are in essence the persons who step into your shoes.

Anyone you name for these important positions needs to be level-headed, good with money management, not a chronic procrastinator, and sturdy enough to say 'no' if necessary to any overreaching by the beneficiaries, etc.

Again, your family members can be named for these positions. Your documents can also give persons the power to remove and appoint others for these positions.

The Mechanics of Your Core Documents

For readers who have the tolerance to continue reading more technical points in this newsletter, the following outlines the operation of the core estate planning documents for a married couple, which for many clients will be a Declaration of Trust for each spouse. I referred to this Declaration of Trust above as part of the core package of documents. You can revoke, revise, or change a Declaration of Trust in any manner while you are alive.

The Declarations of Trust will be presently operative and in existence, but in many cases not yet funded. If not sooner, the trusts will be funded at your respective deaths.

The Declaration of Trust for the first-to-die spouse will continue to operate for the benefit of the surviving spouse and after both your deaths for the benefit of your children in continuing trust.

Keep in mind the surviving spouse's own Declaration of Trust also will continue in existence after the first spouse dies. Thus, both of your Declarations of Trust will be operative

for the benefit of the surviving spouse for his or her remaining lifetime. The two trusts can be combined after the surviving spouse's death for the benefit of your children.

Here is an important point. While you are alive the primary purpose of your Declarations of Trust is for use of the trusts in the event one of you later becomes incapacitated.

For example, if John's incapacity were to occur, Jane will become the successor trustee of John's Declaration of Trust. Jane will also have the related power under John's financial power of attorney to transfer John's property into his Declaration of Trust in order for Jane to hold and manage John's property in his trust.

As trustee of John's Declaration of Trust, Jane will be treated under the law as the legal owner of John's Declaration of Trust property, with Jane's ownership of John's trust property governed by the terms of John's Declaration of Trust. Jane can then deal as owner with the trust property (as to investments, sales, and other transactions under your sole ownership authority as trustee).

By contrast, if John is incapacitated and he does not have the above Declarations of Trust set-up in place, Jane's only other options are to manage John's property as either (i) John's agent under his financial power of attorney or (ii) under a court-managed guardianship for John's property. These two options (compared to Jane being John's trustee) will be much more difficult for Jane and will present her with numerous administrative hurdles and problems, compared to the trustee set-up.

The series of steps above are the same if Jane predeceases John or becomes incapacitated.

Your IRAs and 401(k) plans cannot optimally under the tax law be a part of this Declaration of Trust set-up and will operate after your deaths by their own account beneficiary designations, etc.

The pour-over Last Wills and Testament are companion documents to the Declarations of Trust and apply narrowly to include the naming of guardians for minor children and to direct that any estate property be poured-over into the Declaration of Trust. These Wills then fall by the wayside.

Of course the financial powers of attorney (particularly as illustrated above for the transfer of property into an incapacitated spouse's Declaration of Trust) and heath care proxies are necessary to round out this package of estate planning documents.

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[1] Examples from University of Texas Law School Professor Stanley M. Johanson at the 2011 Southern Federal Tax Institute in Atlanta, September 23, 2011.