

THE WILSEY LAW FIRM

ESTATE PLANNING GUIDEBOOK

A Guide to Assisting your Estate Planning Attorney
with the Preparation and Maintenance of an Estate
Plan that will protect you and your family.

A Publication of:



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Introduction

What is Estate Planning? Some people define it as a will, or a trust, or a life insurance policy, or one of dozens of other documents and products that are purport to pass assets from one generation to the next.

However, Estate Planning is much more than any single document or product. Rather, an Estate Plan is a *plan* designed to protect you and your family in the event of your incapacity or death. An Estate Plan not only incorporates documents, such as wills and trusts, but also puts into place a map for how those documents will work to protect your kids and other loved ones.

So that gets us back to the question of “What is Estate Planning?” While I suppose the answer differs from family to family, here’s a definition I use as a starting point. See if it works for you.

Estate Planning is the process of putting forth a plan and documents that support such plan that will allow you to:

- Control your property while you are alive;
- Protect your property from creditors, while you are alive and after your death;
- Take care of you and your loved ones if you are disabled;
- Give your assets to whom you chose in the manner in which you choose; and
- Do all of the above while saving every last tax dollar, court cost, and attorney fee possible

That pretty much encapsulates Estate Planning. The documents needed may be different, and the provisions within those documents will certainly be different, from family to family. However, whatever your specific documents needs, every families needs the items listed above.

The purpose of this Estate Planning Guidebook is to give you the information you need to effectively assist your estate planning attorney with the preparation of your estate plan. The attorney-client relationship is crucial when it comes to estate planning. A client must be well informed about the options in order to assist the attorney with the preparation of their plan. The attorney must counsel the clients on the ramifications of various choices, in an effort to get the most protective plan possible.

Unfortunately, most Americans have estate plans that are inadequate for their needs, and consist of boilerplate documents designed as a “one-size-fits-all” solution. This is not

realistic, since all families are unique. As a result, it is imperative that your estate plan be designed to fit your unique situation.

I therefore invite you to read through this estate planning guidebook. Please take notes, and formulate opinions about what is important to you and your family. In doing so, you will make the conversation you have with your attorney much more productive, and you will have the reassurance that comes from knowing that your estate plan will provide the best protection possible.

The Family Protection Trust

If you're a Californian, you've probably been told you need a Living Trust. Advertising from a variety of sources would have you believe that the Living Trust is the cure for all that ails you, from probate to the common cold. That may be an exaggeration, but in my opinion, the trust may be one of the most over-sold products on the market.

I don't say this because the Living Trust is bad; per se, in fact, it's my belief that the Living Trust is important for any Californian with over \$100,000 in assets and vital for anyone with assets in excess of \$1,000,000. I say this because many people selling Living Trusts are pushing an inferior product (note that I did not call it a service), which may leave your family in a worse position than if had you done nothing at all.

Yet, if you search online for "Living Trust," you will be bombarded with a million different Web sites, each advertising a Living Trust for various amazingly low prices. There are attorneys who will do a Living Trust for anywhere between \$300 and \$1,500. This usually means the attorney's are running a cheap "trust mill" with underpaid paralegals cranking out boilerplate trust after trust. Usually the client has a cursory, short appointment with the attorney, or he or she may never even meet the attorney at all.

These trusts are the Probate Avoidance Trusts that permeate estate planning currently. Because probate is such a hot button topic, most estate planning attorneys have chosen to hard-sell these trusts solely as a way to avoid the probate process.

However, I'm sure you are wondering if these low price wonder-trusts are worth it. In fact, deep down I'm guessing you know that these Living Trusts must be so inexpensive for a reason. But why? What makes a good Living Trust? What makes a bad Living Trust? And how do you know if you have one that will really protect you and your family?

The purpose of this paper is to answer these questions for you. If you already have a Living Trust, I'm going to provide you with some tips on determining whether your trust will truly protect your family. If you do not have a trust, I'm going to provide you with the information you need to make an informed decision on how to properly protect your family.

The first section of this paper will define a Living Trust. Next, I will outline the problems that most Probate Avoidance Trusts do not address, and I will also outline the way in which a Family Protection Trust™ solves these problems. A Family Protection Trust™ is a trust I've developed to incorporate thorough counseling in order to create a Living Trust

that is tailor-made to your family and will protect you in ways a Probate Avoidance Trust cannot.

If after reading this article you have any questions or would like to set up a Family Protection Trust™ for your family, please contact me directly.

What is a Living Trust?

The first thing we have to do is define just what constitutes a Living Trust. A Living Trust is a revocable (meaning changeable) agreement between a grantor and a trustee to have assets put into the trust by the grantor managed by the trustee for the benefit of the trust beneficiaries.

Now, during your lifetime and the lifetime of your spouse, if you're married, you will likely be the grantor, trustee and beneficiary. This means that you and your spouse will have full dominion and control over the trust assets during your lifetime.

At your death, the trust will be managed by the trustee for the benefit of your successor beneficiaries, who are generally going to be your children (and grandchildren, if applicable). Because the trust owns the property, rather than you, upon your death, the assets owned by the trust can pass to your loved ones without probate. As we will soon see, this is generally a good thing, because probate is time consuming and expensive. However, it seems quite apparent that for most people pitching living trusts, this was the end of the story. I say it's just the beginning.

What are the Problems with Probate Avoidance Trusts?

Why am I, an estate planning attorney, so negative regarding a Living Trust? Again, I'm not. I'm just warning you about the problems with the Probate Avoidance Trust, which constitutes the majority of Living Trusts. I'm warning you that if you do not seek out a qualified estate planning attorney, who practices in a method similar to my Family Protection Planning™ style, you can wind up causing more harm than good. Let's take a look at the problems with most Probate Avoidance Trusts. Then, a little later, I'll show you what to look for in order to ensure that your Revocable Living Trust really works.

Problem 1: Probate Avoidance Planning

As stated, most estate planning attorneys engage in Probate Avoidance Planning. This means that the sole purpose of the trusts they create is to avoid probate. What's probate, and why do you need to avoid it?

Probate is the process by which a court disposes of your assets if you die, either without estate planning documents or with just a will.¹ The problem with probate is that it is (1) LONG, often lasting for 9 to 18 months after your death; (2) EXPENSIVE, often costing 3% to 8% of the *GROSS*² value of your estate; and (3) PUBLIC, as anyone can go to the courthouse and obtain copies of all your probate records, including your will.

With all those calamities, who wouldn't want to avoid probate? In fact, you're probably saying, "No wonder so many attorneys pitch the Living Trust as the solution to all that ails you." However, there is a problem with this standard style of estate planning.

With probate, you get the benefit of court oversight of your estate. There's not likely to be any "funny business." Whomever you wish to obtain your assets will be the person or persons who ultimately benefit from your estate.

With a trust, your wishes are only as good as the trustee who follows them. I have seen instances of unscrupulous trustees stealing assets instead of properly distributing them to the appropriate beneficiaries. If your trust is not completed properly, this can happen to your children.

The point is not to say you should not obtain a trust. You probably should. I'm simply stating that it is not always in the best interest of your family to engage in Probate Avoidance Planning. Family Protection Planning™, which is type of estate planning I've developed, incorporates not only avoiding probate, but also a great deal of additional factors, such as Incapacity Protection Planning™, estate tax planning, Surviving Spouse Protection Planning™, trustee selection, Beneficiary Protection Planning™, the list goes continues. There is so much more to Living Trusts than considered with Probate Avoidance Planning. You need to ensure that you create your trust correctly, or it may be prudent to just let your estate go through probate.

Solution: The Family Protection Trust™

In order to avoid the problems caused by the Probate Avoidance Trust, you should inquire about creating a Family Protection Trust™. A Family Protection Trust extends far beyond Probate Avoidance Planning to deal with a variety of issues that may affect you and your family.

¹ It is a common misconception that a will avoids probate. This is not true. All people who die with a will only have their estates go through probate.

² Note the use of the term gross. This means that you do not subtract liabilities, such as mortgages, from your assets. Therefore, if you have a \$1,000,000 house with a \$999,999 loan, the probate fees are based on the \$1,000,000 gross value, rather than the \$1 net value.

Problem 2: Your Trust is Not Customized

As my wife can attest, I like to buy my suits at Brooks Brothers. However, there's one problem. I'm a size 43 jacket. If you've ever looked for a size 43 jacket, you'll know it's a difficult task. Stores usually have 500 size 42s in every style and color. The same for the size 44s. However, just try finding a size 43. At most, there may be two or three hanging on the wall. Generally, they are grotesque stripe and square patterns that look more like a circus clown outfit than a business suit. Luckily, at Brooks Brothers, for some reason, they carry plenty of size 43s in great styles and colors, and as such, I'm definitely a fan.

However, imagine a store where not only did they not have ANY size 43s, but they only had ONE size period! The size could be that of the average man, say a size 38. Imagine if I went in and was forced to buy a size 38 and forced it to fit me. Of course it wouldn't fit; I'd be bursting through the seams. If a suit does not fit properly, it might be better than nothing, since I'm not naked, but it's certainly not right for me.

This analogy is akin to the craziness that currently afflicts those with Living Trusts. Families are all unique, with different dynamics and distinctive hopes and dreams. Therefore, why do most families settle for cookie-cutter trusts that are designed for the "average family?" It does not make sense, and in fact, can be dangerous.

Solution: A Family Protection Trust is Customized to Meet Your Family's Needs

The process involved in creating a Family Protection Trust™ goes deep into the specific needs of your family. Far from being a cookie-cutter document, your Family Protection Trust™ will be a customized encapsulation of your hopes, dreams, and wishes for your family in the event something happens to you.

Problem 3: Your Trust is Not Funded

Another common mistake deals with the failure to properly fund a Living Trust. To "fund" means to title assets in the name of the trust so that the trust, rather than you, is the legal owner of the trust. Failure to fund your Living Trust will result in those non-funded assets being subject to probate.³ This is remarkably common, since most trust peddlers and attorneys do not assist you with funding your trust or do so only to a limited extent. This seems ironic since the main purpose of their practice is Probate Avoidance.

³ Your estate will only go to probate to the extent the sum of your assets not in the trust, and not passing via a beneficiary designation form, exceed \$100,000.

The result is that many trusts end up in probate court for the sole purpose of getting the probate judge to put the assets into the trust. This defeats the purpose of setting up the trust, since most Living Trusts are done for the sole purpose of avoiding probate.⁴

Solution: Our Funding Process for the Family Protection Trust™

In order to make sure our Living Trusts actually work, I include in the price of the Family Protection Trust the assistance of our funding coordinator to fund your trust.⁵ This will ensure that your estate plan will be complete. In order to make sure that your trust stays funded, we offer a funding maintenance program, which will ensure that you receive assistance on an annual basis, keeping your trust properly funded. We are so confident in these services that we will even do your probate for free if any of your assets are outside of your trust at your death.⁶

Problem 4: Your Trust Does Not Deal with Incapacity Adequately

As I have said before, the main problem with most Probate Avoidance Planning is that the trusts these attorney prepare only deal with probate. That's like buying a new car that can only drive in reverse. Yes, driving in reverse is very important, but there is much more you need a car to do for you.

The main problem most trusts do not deal adequately with is incapacity. You are six times more likely in any given year to become incapacitated than die in any given year. If you are incapacitated without proper planning, your estate could go through a lifetime probate, called a "conservatorship." Just like probate, a conservatorship is (1) LONG; (2) EXPENSIVE; and (3) PUBLIC.

Doesn't it make sense to set up your Living Trust so that a conservatorship is highly unlikely to occur? Unfortunately, with Probate Avoidance Planning, this is not always the case.

Solution: Incapacity Protection Planning™ with a Family Protection Trust™

Planning for incapacity properly requires thought on your part with guidance from your attorney. I try to provide clients with a number of options to (1) determine your specific

⁴ A trust that goes through probate does give you the benefit of determining where your assets will go upon your death. However, you could do this with a will, which is generally less expensive than a trust.

⁵ We include ten hours of assistance in the price of the Family Protection Trust™. If more time is necessary, it will be billed at our paralegal rates.

⁶ Adherence to our Funding Maintenance Program is required to receive this benefit.

definition of incapacity; (2) determine who will take care of you in the event of your incapacity; and (3) determine how they will take care of you.

Problem 5: You Do Not Have a Bypass Trust

At the death of the first spouse, everything that passes to the surviving spouse is done so on a tax-deferred basis, meaning that no estate taxes are due until the death of the surviving spouse. That sounds great, right? WRONG!

The problem is that if you leave everything at the death of the first spouse to the survivor, you miss the opportunity to use the estate tax exemption of the first spouse who passes away. In 2008, this exemption is \$2,000,000 per spouse. With the estate tax rate of 45%, this means you lose the opportunity to save your loved ones \$900,000 in estate taxes.⁷

A Bypass Trust is a trust that allows the use of the deceased spouse's estate tax exemption. The surviving spouse can continue to use these assets, but he or she will be exempt from estate taxes at the death of the surviving spouse. This way, both spouses will get to use their estate tax exemption.

There are, to my knowledge, at least 12 different types of Bypass Trusts.⁸ Unfortunately, most trusts I see use a method that may cause unnecessary capital gains taxes at the death of the first spouse. This is an extremely problematic scenario, and you need to make sure you have the correct type of Bypass Trust.

Solution: A Family Protection Trust™ with a Bypass Trust

If your assets are large enough, you will need a Bypass Trust to save estate taxes upon your death. We will also ensure that your Bypass Trust will avoid unnecessary capital gains taxes upon the death of the first spouse.

Problem 6: There is No Protection for the Surviving Spouse

I'm seeing a great deal of cases where a surviving spouse is left vulnerable after the death of the first spouse. Questions arise, especially from one or more of the couple's children, regarding the surviving spouse's use of the family assets after the death of the first

⁷ There are two real rough assumptions I'm making that I want to acknowledge. First, I have no idea what the estate tax exemption will be at the death of the first spouse. I'm just using 2008 numbers. Second, the \$900,000 figure assumes both spouses die in 2008. Naturally, if the surviving spouse lives for a number of years, this figure will grow.

⁸ More precisely, these are ways of putting assets into the Bypass Trust.

spouse. Unfortunately, the underlying purpose of these inquiries, in my humble opinion, seems to be a desire by said child to protect their inheritance.⁹

In addition, there is a huge increase in the case of elder abuse where thieves and charlatans target older widows and widowers in an effort to separate them from their assets. Witness the explosion in growth of the “Elder Law Abuse” legal field, where attorneys are trying to deal with these abuse cases after the fact, sometimes successfully, sometimes not.

Wouldn't it be nice to have a way to protect yourself and your spouse against these problems before they arise?

Solution: Spousal Protection Planning™, Planning with a Family Protection Trust

The Family Protection Trust, through Spousal Protection Planning™, will help ensure that (1) your spouse is financially protected after your death; (2) your spouse is protected from creditors and predators after your death.

Problem 7: No Protection if Your Spouse Remarries After Your Death

There are a significant number of widows and widowers who remarry after the death of their spouse. Most trusts do not address this at all. However, upon remarriage, your spouse's new significant other may acquire rights in your property. There are two problems with this.

First, what happens if the new significant other is just after your spouse for the money? Or what happens if the relationship starts with the best of intentions, only to fall apart later? Wouldn't you like to make sure your spouse is protected?

The other problem is the fact that your children could lose some or all of their inheritance to the new spouse and/or the new spouse's children if you are not careful. Without proper planning, your assets may end up going to someone you don't even know.

Solution: Spousal Protection Planning™ with the Family Protection Trust™

The Spousal Protection Planning™ that is included in the Family Protection Trust will help ensure that your spouse and children are protected if your spouse decides to remarry.

Problem 8: Improper Choice of Trustee

⁹ Rest assured in your faith in humanity, as I am seeing this on a small number of estates percentage wise. However, I am seeing an increase in this problem, which leads to my inclusion in this article.

One common mistake I see is an improper choice of successor trustee. Usually, in my experience, this happens where the eldest child is put in charge of dividing the assets up at the parent's death and distributing them to the other children.¹⁰ I don't think you should do this for two reasons.

First, there is the chance your eldest child will not be entirely honest with the other siblings and either keep extra assets for themselves or "cherry pick" the best assets. For instance, I once saw an estate where the eldest sibling was chosen as trustee. There was \$500,000 in cash and \$500,000 in a taxable annuity. The eldest sibling/trustee saw it appropriate to distribute the cash to himself and the \$500,000 tax problem to his sibling. That's not exactly an equal distribution in my book.

Second, and more likely, even if your one child you've selected as trustee is perfectly honest, they will face resentment from their other siblings, who view themselves as slighted. For instance, when I was a child, my parents used to put me in charge of my younger brothers when they'd go out to dinner. No matter how fair I was, my brothers would always give me grief to the point where I would've rather had my parents hire a babysitter.¹¹ Think age changes things? Think again. I see sibling feuds time and time again in my practice.

The same thing applies to selecting a friend or other relative as trustee. The level of mistrust that seems to arise astounds me, but I guess this is simply human nature.

This is such a common problem that you really need to think about with your attorney. This is where the Family Protection Planning™ style of estate planning, which seeks to dig deep into your family dynamics, has a distinct advantage over the traditional "Probate Avoidance Planning."

On one final note on trustee selection, I cannot think of a good reason to select the attorney who drafts your trust as your trustee. Many attorneys seem to have taken to naming themselves as successor trustee for their clients. For a variety of reasons this is not a good idea. While I'm sure there are some attorneys out there who are good trustees, I am against this practice, and I strongly urge you to be suspicious of this.

Solution: Proper Selection of Trustee Based on Your Family Dynamics

It is essential to pick the right trustee. Your trust will not work if he or she does not follow your directions properly. Family Protection Planning will help ensure that you

¹⁰ This would also apply if you select one of your other children as the sole trustee.

choose the right trustee for you and your family. You may be surprised at who you end up selecting!

Problem 9: No Common Trust for Minor Children.

One big problem I see with Probate Avoidance Trusts is that client with minor children split up their inheritance evenly among their kids immediately when they die. The problem if you do this is that your younger children may not get the same advantages with respect to education, health care, and general maintenance as the older ones, resulting in an unequal outcome.

Additionally, think about it for a second. When you spend money supporting your kids, do you divide the resources you use into a separate share for each child, making sure that if you spend some money on one child, the other children get the same amount? To put it another way, if you had a child with an illness, would you quit spending money on their medical expenses because it eats into your other children's share of the inheritance? You probably wouldn't. It makes no sense to do this in the event you and your spouse die before your children are able to support themselves.

Solution: A Family Protection Trust™ with a Common Trust for your Children

A common trust makes sure that your assets are held in a common pool for your children until the youngest reaches a certain age (usually 25, although it could be any age) or graduates college. This ensures that your younger children get the same benefit from your assets as your older children.

Problem 10: No Protection for Children

There are so many factors that can cause your children to lose their inheritance. Poor spending, creditors, bankruptcy, lawsuits, and divorce are a few of the factors. Wouldn't you like to make sure your kids get the full benefit of their inheritance?

The problem is that most trusts leave an inheritance outright to your children once they reach a certain age or maybe half when they reach age X and the other half when they reach age Y. The problem is that the moment assets are distributed outright to your children, the problems listed above can happen. The Probate Avoidance Trust does not protect your children at all once assets are distributed.

Solution: The Beneficiary Protection Trust™

In order to properly protect your children, you need a Family Protection Trust with special provisions, creating trusts that last for the lifetime of your children. This is called a Beneficiary Protection Trust and will ensure that your children's inheritance is protected from frivolous spending, creditors, divorce, and lawsuits.

I've written an article on Beneficiary Protection Trusts called "Beneficiary Protection Trusts: Protecting Your Life's Work and Your Children's' Inheritance." This article goes in depth into the Beneficiary Protection Trust. You can access this article by contacting my office if you do not have a copy already.

Problem 11: No Method for Changing the Trust if Circumstances Change

What happens if the trustee you choose runs amok or refuses to make distributions to your children? Shouldn't there be a way to remove them? What happens if California changes its laws to tax trusts at a 70% rate? How can you move your trust to a low tax state? What if laws change? What if your circumstances change?

The Probate Avoidance Trust does not answer these questions. Instead, after your death, the Probate Avoidance Trust requires your children to seek the assistance of the Probate Court. This is an expensive, lengthy process, and there is no guarantee that the Probate Court will even grant their request. Your Living Trust needs to provide a better mechanism for change.

Solution: The Use of a Trust Protector with the Family Protection Trust™

The Family Protection Trust™ is designed with change in mind. We include a Trust Protector, who is a non-beneficiary, such as a friend, family member, CPA, or attorney, who can remove and replace the trustee if they are not doing what your trust requires them to do.¹² In addition, the Trust Protector can switch the trust to another jurisdiction if the need arises because of taxes or another reason. The Trust Protector is also given certain powers necessary to update your trust should circumstances change.

The Solution to all these Problems is the Family Protection Trust™

As you may have gathered, I call my practice Family Protection Planning™. What does this mean? Well, when I look at you as a client, I see more than an estate that needs to avoid probate. The key difference between probate avoidance planning and Family Protection Planning™ is my function as a counselor. Because of my wealth of experience in estate planning, I have a great deal of ideas on how estate plans should be customized

¹² If you want, you can give this power to your children as well. However, you should realize that if you do this your child can frustrate your wishes by hiring a trustee who will do whatever they want.

for each individual family. The goal is to ensure that the family members are protected to the best extent possible, as opposed to just avoiding probate after your death.

Again, the problem with Probate Avoidance Planning and the ensuing Probate Avoidance Trust is that they really deal with just one thing (maybe two things if it includes a Bypass Trust):

- Avoiding probate
- Reducing estate taxes (while possibly increasing capital gains taxes)

Yes, avoiding probate and reducing estate taxes are important, but there are other issues that affect you that are dealt with in the Family Protection Trust™, such as:

- Family Protection Planning™, rather than Probate Avoidance Planning
- Customization to fit your family needs, rather than a cookie-cutter trust out of a form book
- Incapacity Protection Planning™, protecting you and your family in the event of your incapacity
- The funding of your trust to ensure it actually avoids probate
- A Bypass Trust to ensure you save estate taxes at the death of the first spouse without incurring unnecessary capital gains
- Surviving Spouse Protection Planning™, protecting your spouse and children against issues arising after your death
- Protection for your spouse and children if your spouse remarries after your death
- A Common Trust to protect minor children
- Protecting your children from poor spending, creditors, lawsuits, and divorce with a Beneficiary Protection Trust
- Proper Selection of a Trustee to ensure your plan is carried out properly
- The use of a Trust Protector to ensure your estate plan changes as your needs change, even after your death

I've developed the Family Protection Trust™ through careful research in California law and the practices of estate planners throughout America. As a result of my efforts, I'm confident that the Family Protection Trust™ is the best protection you can have for you and your family.

The Beneficiary Protection Trust

Having a Family Protection Trust™ is certainly the foundation of an excellent estate plan. During your life, the Family Protection Trust™ will protect you from the expense and loss of dignity associated with a Conservatorship. After your death (and the death of your spouse, if you are married), your trust will pass to your family without the need for Probate.

However, you should also consider what will happen to the money you leave your loved ones. It might surprise you to know that often recipients of an inheritance are negatively affected by the wealth they inherit. You may not think that this applies to your family. If not, then you can use your Family Protection Trust to distribute assets after your death once your beneficiaries reach a certain age. However, please read below, and if the concerns addressed in this section both you, then you need a Beneficiary Protection Trust™.

This section details problems faced by most successful families that are not addressed by most Living Trusts and most estate planning attorneys. The solution to these problems comes in the form of the Beneficiary Protection Trust™, a unique addition to the Family Protection Trust that allows you to leave your loved one's inheritance in a trust for the duration of their lives. This will protect their inheritance against creditors, divorce, lawsuits, and general mismanagement.

The Problem

Let's first look at the problems that affect the inheritance you will leave your loved ones. While this article deals specifically with an inheritance to be received after your death, these principles apply to gifts you give your children as well.¹³

Lack of Incentive and Blown Inheritances

There are two major non-creditor related problems to inherited wealth: (1) a lack of incentive for beneficiaries; and (2) inheritances that are consumed in rapid fashion. It is my belief that these two problems are inherently related. I will collectively refer to this problem as "Affluenza," a term I did not coin but which encapsulates the problem in one beautiful catch phrase.

¹³ You can certainly form an Irrevocable Beneficiary Protection Trust to deal with gifts you make during your lifetime, which will have very similar characteristics to the trust described herein.

If you are not careful, you could provide disincentives to your children to work and accomplish goals. While living off of inherited wealth may seem like a great idea, it can actually be a horrible burden for wealthy heirs. In fact, it can lead to feelings of low self-worth due to a lack of a sense of accomplishment. For example, Psychologist Gary Buffone, author of the book *Choking on the Silver Spoon*, writes that an inheritance can "devastate otherwise healthy children, even children who are adults before they find out that they have been made rich."

It is also commonly understood that inherited wealth is often blown, leaving successive generations in the same place as the family member who created the wealth in the first place. In fact, in America, the average inheritance is completely consumed in less than a year. Wealthier families may see their fortunes last a bit longer, but the problems of beneficiaries rapidly consuming wealth, leaving future generations to fend for themselves, is very real.

Have you ever heard the saying "Shirtsleeves to Shirtsleeves in Three Generations"? There's a version of this proverb in every culture across the world. The basic idea is that the first generation will work hard to create the wealth, but the successive generation, given disincentives by the wealth, never learns to create wealth of its own. The result is that by the third generation, the family is poor again and must start over.

For instance, take the Vanderbilt Family. Cornelius Vanderbilt is regarded as the second wealthiest person United States history, with a fortune that in today's dollars would exceed \$143 billion. When he died in 1877, his last words were "Keep the Money Together." This did not happen. Less than 100 years later, in 1973, the first Vanderbilt family reunion was held at Vanderbilt University. There was not a millionaire present, as the family had squandered all its wealth.

This might seem like a problem that only affects the Vanderbilt's and Rockefeller's of yesteryear and the Gates' and Buffett's of today. However, with the growing "middle-class millionaire" population in America, a phrase coined by Russ Alan Prince, the problem of inherited wealth is becoming more dramatic.

The median income in America in 2006 was \$48,201, according to the U.S. Census Bureau. If you leave a beneficiary the sum of \$1,000,000 with instructions to give that beneficiary 5% of the \$1,000,000 per year, you will give that beneficiary an inheritance that will provide them with an annual income of \$50,000, which exceeds the income of

the average American.¹⁴ Of course, this assumes that this inheritance is given in a way such that your beneficiary will not simply spend it right away. What effect will such an inheritance have on your beneficiary?

Creditors

I use the term Creditors to loosely refer to any person who can use a court of law to compel your beneficiary to give up his or her inheritance. This could happen due to any of the following:

Bankruptcy

Young folks today are often saddled with debt. Bankruptcy filings are on the rise, especially for young adults saddled with debt. These bankruptcy filings are not coming from deadbeats. Did you know that 91% of all bankruptcy filings result from the loss of a job, a health problem, or a divorce? This can happen to your children, even if they lead respectable lives.

Lawsuits

The statistics are alarming. A new lawsuit is filed every two minutes in America. In every year between 2001 to 2006, growth in lawsuits exceeded growth in Gross Domestic Product by at least 2%. In 2006, the cost of lawsuits worked out to \$880 per American.¹⁵ The problem is only growing, with no end in sight. Inherited wealth is not immune to these threats.

Divorce

In America, it is commonly stated that ½ of all marriages end in divorce.¹⁶ It is estimated in some studies that this rate is even higher in Southern California, possibly 60% to 75%.¹⁷

¹⁴ Assumes 8% growth. The figure of 5% allows for a 3% inflation adjustment to ensure that the beneficiary receives roughly the same amount over time.

¹⁵ 2006 Update on U.S. Tort Cost Trends, a study performed by Towers Perrin Tillinghast.

¹⁶ Did you ever wonder where this oft-cited statistic comes from? Me too. I did some research and found out that it comes from an analysis of numbers provided by the U.S. Department of Health and Human Services Centers for Disease Control and Prevention, which stated that the annual divorce rate was 4.1 per thousand population in 2001, while there were 8.2 marriages per thousand in that same year. Divide one by the other, and you get 50%.

In California, inherited property is technically separate property, and is not available for the ex-spouse. In reality, it is my experience that most people who inherit wealth co-mingle the property with their spouse, causing it to become a community property. This leads me to advise clients to assume that if they leave an inheritance outright to their children, it will become available to the ex-spouse in the event of a divorce. Inheritances can often become a source of contention in divorce proceedings.

Loss of Government Benefits

Statistically, 1 out of every 5 Americans is disabled.¹⁷ Those Americans who are unable to work because of their disability are entitled to receive income and health care benefits.

If one of your family members currently receives government benefits because of a disability or becomes disabled in the future, an inheritance can ruin his or her chance to receive needed government benefits for living and medical expenses.

While the income benefits afforded by the government to disabled Americans are modest, the health care benefits are important because your family's inheritance can be decimated by increasing health care costs.

Lack of Distribution Instructions

It has long been the practice of trust attorneys to meter out distributions to young beneficiaries in stages, or at least until they reach a certain age. This is why most trusts say that a beneficiary will get ½ at age 25 and the other ½ at age 30, or some variation thereof. Some wealthy people, fearing that one of their children will blow his or her inheritance, decide to leave the inheritance to this child in trust, while leaving the other children an outright inheritance, free of trust. While these types of provisions are great for protecting beneficiaries from completely blowing the inheritance, it also, at the same

¹⁷ I'm not sure about these statistics, which I found reported on so many Web sites that I'm not sure of the original site. However, since California is one of the few states that does not report divorce statistics, I am not sure how they came up with this number. Be that as it may, I am sure, being a Southern Californian, that many of my acquaintances have got or are getting a divorce, so I suspect the accurate number is surprisingly high, even if it is not the 60% to 75% number frequently repeated.

¹⁸ This statistic is from the Congressional Committee findings for the Americans with Disability Act of 1990.

time, has led to an influx of trust litigation, as these beneficiaries are increasingly suing trustees for a perceived lack of distributions from the trust.

As a result, there is an influx of trust litigation cases into California courts. This eats up inheritances paying for court costs and attorney fees. More importantly, the trustee may actually not be following your actual wishes, leading your beneficiary to obtain less of a benefit from his or her inheritance than you had intended.

To reiterate, the three problems addressed above are:

1. Lack of Incentives and Blown Inheritances
2. Lack of Protection Against Creditors
3. Lack of Instructions for Distributions

The Real Question Is Whether Your Trust Prevents These Problems¹⁹

So, will your trust protect your family against the problems listed above? In most of the trusts I have reviewed, the answer is decidedly “NO.” These documents may deal with technical issues involving avoiding probate and conservatorship, but they really don’t deal at all with protecting beneficiaries from themselves and others. As a result, your loved ones can lose everything.

Here’s a list of what a trust must address in order to protect your family against the three problems listed above:

A Trust Must Last for the Lifetime of Your Beneficiary.

The first step for avoiding the three problems listed above is that you must never leave an outright inheritance to your beneficiaries. Instead, you must leave it to them in a trust for the duration of their life.

The main reason for this problem is that beneficiaries are given control and access to a vast amount of unearned wealth. This unfettered access and control leads to Affluenza. To combat this, we must separate the beneficiary from the inheritance. We accomplish this by leaving the assets in the trust for the lifetime of the beneficiary.

¹⁹ Notice that I assumed you have an estate plan, i.e., a trust or will. If this is not the case, you are not protected against these problems.

To clarify, this means that instead of your beneficiary's inheritance going into his or her bank account at a certain age or in stages over a course of years, the full inheritance will remain in trust for the duration of his or her life. It will then pass to his or her descendants upon his or her death. You can even give your beneficiary the power to decide to whom the trust goes upon his or her death. However, the main point is that the beneficiary will never actually own the trust assets outright.

A Trust Must Place Control with a PROFESSIONAL Third Party.

The next feature of your trust is that the assets must be controlled by an independent third-party professional trustee.

This is probably the most resistance I get from my clients. Many want their children to be in control of their inheritance. This is fine. However, realize that as an estate planning attorney, I try to work in absolutes. If you become a client of mine and follow the advice given in this paragraph, I have the utmost confidence that your plan will have the best possible chance for success. If you do not follow the advice, I cannot make a strong prediction. In fact, statistically, your loved ones will likely fall victim to the problems mentioned in this article. If you can live with that likelihood, that's fine, and we can still design your Beneficiary Protection Trust to protect them from creditors, which is a huge issue.

If you follow my advice, the next important step is to pick an appropriate trustee. The trustee is responsible for managing the trust, making distributions to beneficiaries, and complying with federal and state tax requirements. In my opinion, the law regarding trusts, and the potential liability surrounding service as a trustee, make a layperson an inappropriate person to serve as a trustee.

Many clients request that a family member, such as a brother or sister, serve as trustee. Besides the incredible complexity, this introduces a bad family dynamic that puts the older family member (aunt or uncle) in charge of your beneficiary's inheritance. This generally makes the younger family member bitter at the person they see as "hoarding" their rightful inheritance.

Instead, I suggest you choose a professional trust company to serve as trustee of your trust. These companies have a great deal of experience managing trusts, with billions of dollars under management. They have knowledge of the complex laws that require tax filings, accountings, and other administrative tasks. They have the ability to follow the

instructions of your trust document without emotional family ties that may affect their judgment.

A Trust Must Contain Specific Instructions for Distributions

One of the biggest problems with trusts is that they fail to contain specific instructions for making distributions to your beneficiaries. As discussed above, the result is a level of animosity between the beneficiary and trustee, because the beneficiary feels the trustee is being stingy with distributions.

In lifetime trusts, this is an especially big problem, since the trust lasts for the lifetime of the beneficiary. Usually, it is just the result of a lack of specific instructions within the trust. Often, the client wants to restrict distributions to prevent the beneficiary from the negative implications of too much of an inheritance.

As such, your trust absolutely must contain specific instructions for making distributions to your beneficiaries.

What type of instructions? For starters, I like to specify that your beneficiary will get a specific percentage of the trust assets per year as a distribution. This method is commonly referred to as a Uni-Trust. For example, if your beneficiary gets a 4% Uni-Trust, and the trust assets are worth \$1,000,000, he or she will get the sum of \$40,000 per year.

With Uni-Trusts, I like to use the figure of 4% to 4.5%. Assuming that the trust grows in excess of this distribution, this allows the distributions to increase to account for inflation. For instance, if the trust grows at 8% (hardly an over-the-top growth rate), a 4% uni-trust will pay the same amount year after year assuming 4% inflation.

In addition to the Uni-Trust, you should specify whether you would like to make additional specific distributions. These distributions might include:

- Education
- Housing
- Business Loans
- Weddings
- Replacing Income for a Stay-at-Home Parent
- Income Matching
- Withholding Provisions

The main point is that these distributions should be incorporated into your trust to make sure your instructions are clear. The consequences for failure to do so can be great because it can decimate the trust assets due to fighting amongst the beneficiary and the trustee.

A Trust Must Be Designed to Protect Assets from Creditors

I have already discussed that if you leave an inheritance outright to your beneficiary, he or she can lose that inheritance to creditors. It is a shame that many beneficiaries lose their inheritance to outside parties. This does not have to be the case.

While most trusts leave assets outright to beneficiaries, I have come across a few that leave assets in trust for the lifetime of a beneficiary. Usually this is because that beneficiary is addicted to drugs or alcohol or is otherwise unable to manage their assets. Isn't it ironic that the act of leaving the assets in a trust actually gives them an asset protection benefit?

However, most of these trusts do not go far enough. They include language that gives the beneficiary the absolute right to compel distributions in certain circumstances. This is often the case in trusts that require distributions for the "health, education, maintenance, and support" of the beneficiary. Often this language is included because the drafting attorney does not understand this distribution standard is really used in a certain circumstance to avoid negative estate tax consequences. Unfortunately, this provision is not only unnecessary but actually detrimental.

There is a whole body of case law on what provisions are necessary to make an asset protection trust as protective as possible for beneficiaries. Unfortunately, most attorneys have never read these cases and do not understand the provisions necessary to make a trust as protective as possible.

A Trust Must Protect Potential Government Benefits

The one thing we know for sure about the lives and needs of your beneficiaries is that they will change. Nowhere is this more prevalent than in the circumstance of one of your beneficiaries becoming disabled in the future and becoming dependent on government benefits for his or her health care expenses.

Unfortunately, health care expenses for disabled persons can be astronomical. As such, it is imperative that beneficiaries have the ability to access government benefits to pay for

such expenses. However, if they have an inheritance, it will likely be counted as a resource to the beneficiary, and they will lose their government benefits.

The only way to avoid this is through a Special Needs Trust. This is a supplemental trust that supports a beneficiary by supplementing the needs addressed by government benefits. However, how can you know now whether a beneficiary will be disabled in the future? Certainly, it does not make sense to leave assets to a Special Needs Trust now for healthy beneficiaries, because these trusts are more restrictive than a normal lifetime trust.

As such, your trust should contain a provision that will allow the trust to “morph” into a Special Needs Trust should the beneficiary’s circumstances require. This way, the trust will be a normal trust, as discussed in this article. However, should circumstances warrant, the trust can transform into a Special Needs Trust if and when the need arises.

The Distribution Provisions Must Not Conflict with Asset Protection Provisions

One problem with the above requirement that you include specific provisions regarding how to distribute the trust assets is that this requirement often frustrates the asset protection benefits of the trust.

For instance, say you require your trustee to make a distribution to allow your beneficiary to purchase a house. What if the beneficiary gets sued right before the distribution is to be made? That distribution will go to his or her creditor because the creditor is entitled to any interest in a trust that a beneficiary can force the trustee to make.

As such, your trust must be drafted such that the Distribution Provisions do not frustrate the Asset Protection benefits of your trust. You cannot force a trustee to make distributions. You must only “request” that the trustee make such distributions.

If your distribution orders are only a request, how can you make sure the trustee actually makes the distributions? How can you be sure that your beneficiary will receive the full benefit of what you intended to give him or her, unless they sue the trustee? The answer is next.

Your Trust Must Have a Way to Remove and Replace the Trustee (Other Than by a Beneficiary)

So, if your trust only “requests” that your trustee make a distribution but does not require it, how do we know the trustee will follow your instructions? After all, all of the asset protection in the world is useless if your beneficiary does not benefit from your trust in the way you intended.

The solution is to make sure there is a legitimate way to remove and replace your trustee. But it is not that simple. The instinct is to allow the beneficiary to remove and replace his or her trustee. You’ll see this provision in many trusts. However, you must realize that if you put this provision in your trust, you give your beneficiary *carte blanche* to select a trustee that will do what he or she wants.

In fact, in trusts in which the client wants his or her beneficiary to serve as trustee, I often convince the client to just give the beneficiary the right to remove and replace a trustee, which gives extra asset protection while at the same time allows the beneficiary to retain control.

Instead, you should choose an independent party who has the ability to remove and replace the trustee. This party is often referred to as a Trust Protector.

The Trust Must Have a Trust Protector

In order for your trust to work and really protect your beneficiaries, a Trust Protector plays an important role. The first role is that of mediator between the beneficiary and trustee. More and more, beneficiaries are resorting to suing a trustee whenever they have a dispute.

A Trust Protector serves as an alternative to Trust Litigation. Sitting on the proverbial same side of the table as the beneficiary, the Trust Protector can hear the grievances of the beneficiary, counsel him or her as to whether the concerns are legitimate, and address those concerns with the trustee. If necessary, when a solution cannot be worked out, the Trust Protector can make the decision to remove the trustee.

However, the main thrust of the Trust Protector is to make the beneficiary understand the difficult duties of the trustee and make sure that the beneficiary understands your intent in creating the trust. While a properly designed trust will eliminate much of the animosity toward the trustee through clear instructions, a Trust Protector is still essential to resolving disputes as they arise.

Your Trust Must Be Able to Change Jurisdictions

I must confess that recently I've had state income taxes on my mind. I've heard that California is considering raising income tax rates from the ridiculous 9.3% to an incredible 11%!!! Now you, as a resident of California, cannot reduce your income taxes by forming a trust in another state. However, it may be prudent for your trust beneficiaries to have their trust in another state, such as South Dakota or Nevada, which do not have state income taxes.

Most trusts don't allow for this. If your trust does not allow for this, I suppose the only way to do so would be through a court order. This being the case, I'm not confident that a court would allow the trust to change jurisdictions for the sole purpose of reducing income taxes.

As such, your trust should contain a provision allowing your Trust Protector to change the jurisdiction of the trust to another state, or even out of the country entirely if that makes sense. This flexibility could save your loved ones a great deal of tax dollars in the future.

All These Elements Must Be In Place for the Trust to Work

The items discussed above are designed to work in unison rather than individually. As such, it is important that we review these elements that are essential in making sure an inheritance is truly protected and will really benefit your loved ones. Here's the list:

- A Trust Must Last for the Lifetime of Your Beneficiary
- A Trust Must Place Control with a PROFESSIONAL Third Party.
- A Trust Must Contain Specific Instructions for Distributions
- A Trust Must Be Designed to Protect Assets from Creditors
- A Trust Must Protect Government Benefits
- The Distribution Provisions Must Not Conflict with Asset Protection Provisions
- Your Trust Must Contain a Way to Remove and Replace the Trustee (Other Than by the Beneficiary)
- The Trust Must Have a Trust Protector
- The Trust Must Allow for a Change of State Jurisdiction

The Solution: Beneficiary Protection Trust

The Beneficiary Protection Trust is something I've developed to protect your family from losing their inheritance for any of the above reasons. This trust is designed to be the beneficiary of your Revocable Living Trust. At the time of your death (and your spouse's, if you're married), your Beneficiary Protection Trust will make sure that your loved ones enjoy their inheritance for the duration of their lives.

Benefits of the Beneficiary Protection Trust

The Beneficiary Protection Trust offers the following benefits:

- A Trust That Will Last for the Lifetime of Your Beneficiary

Your Beneficiary Protection Trust will make sure that your loved ones receive the full benefit of their inheritance and that it is protected against Affluenza as well as creditor claims. In fact, my extensive research into California law leads me to the conclusion that the Beneficiary Protection Trust is the most powerful asset protection device allowed under California law. It offers the best chance possible of making sure that your loved ones receive the full benefit of your legacy.

- A Trust Must Place Control with a PROFESSIONAL Third Party.
As discussed above, a third-party professional trustee is important in making sure your trust instructions are followed and that the full benefits of the asset protection provisions of your trust are realized.

This point is obviously contentious. You may come to the conclusion that you would rather have your child manage his or her own trust. Fair enough. If that is the case, we can design a Self-Directed Beneficiary Protection Trust to incorporate the asset protection features to the greatest extent possible. However, I cannot accurately predict whether the instructions you leave in your Self-Directed Beneficiary Protection Trust will be followed, since your child has the full decision-making authority over his or her trust. If you are comfortable with this, a Self-Directed Beneficiary Protection Trust may be fine for your beneficiary.

- A Trust Must Contain Specific Instructions for Distributions

In order to avoid conflict between your beneficiary and trustee, we will incorporate specific distribution instructions designed to spell out when and how distributions are to be made. In addition, we will spell out circumstances when distributions are NOT to be made, such as circumstances when your beneficiary is addicted to drugs and/or alcohol and is using his or her inheritance to hurt him or herself.

- A Trust Must Be Designed to Protect Assets from Creditors

I've undertaken a great deal of research and review of California law, as well as the laws of other jurisdictions. I'm confident that to the greatest extent possible, the Beneficiary Protection Trust will protect your family against losing their inheritance to creditors, divorce, and lawsuits.

- A Trust Must Protect Government Benefits

If your beneficiary is currently disabled and is receiving Government Benefits, or may in the future, you need to strongly consider forming a Special Needs Trust on his or her behalf. Even for healthy beneficiaries, your Beneficiary Protection Trust will contain provisions designed to change the trust into a Special Needs Trust, should the need arise.

- The Distribution Provisions Must Not Conflict with Asset Protection Provisions

Your Beneficiary Protection Trust will make specific distributions, such as the payment of a monthly distribution, in such a way as to avoid the requirement that those payments be directed to another party in the event your beneficiary has creditor problems.

- Your Trust Must Contain a Way to Remove and Replace the Trustee (Other Than by the Beneficiary)

If we cannot remove and replace the trustee, you cannot be assured he or she will follow your instructions. If your beneficiary can remove and replace the trustee, he or she can "trustee-shop" until he or she finds someone who will do what he or she wants. The happy medium is to require the consent of a third-party Trust

Protector whom you trust to remove and replace the trustee, should the trustee not follow your guidelines for distributions.

- The Trust Must Have a Trust Protector

Your Beneficiary Protection Trust will contain provisions appointing a Trust Protector who plays a major role in your estate plan. The Trust Protector serves to add a human element and sits as an advisor to your beneficiary. In addition, he or she serves as a mediator who can resolve disputes between the beneficiary and trustee that could lead to Trust Litigation. In addition, the Trust Protector can make changes to your trust to deal with current trust and tax law changes. This includes the ability to remove the trust to another jurisdiction should tax rates in California be prohibitive at the time of your death.

- Your Beneficiary Protection Trust Will Be Able to Move to Another State.

Your Beneficiary Protection Trust will contain a provision that allows the Trust Protector to switch jurisdictions from California to a more tax-friendly state if the circumstances make sense. This could allow your Beneficiary Protection Trust to keep a great deal more in assets than otherwise allowed.

Putting It All Together

To go back to our central point, Inheritances fail due to the following three reasons:

1. Lack of Incentives and Blown Inheritances
2. Lack of Protection Against Creditors
3. Lack of Instructions for Distributions

If we can protect against these issues to the best of our ability, we can give your wealth the best chance possible of having a positive impact on the lives of your loved ones. You can save your family a great deal of grief and heartache by simply making the effort to plan with a Beneficiary Protection Trust.

The Letter of Wishes

A Roadmap for Your Beneficiary Protection Trust™

If you want your loved ones to receive the most benefit possible from their inheritance, then you should strongly consider leaving your assets in a Beneficiary Protection Trust. If you fail to do this, then you put your legacy at risk to poor spending, creditors, divorce, lawsuits, and a slew of other factors trying to take away your loved one's inheritance.

In leaving your child's inheritance in a trust, and thereby denying them unfettered access to their inheritance, you may be concerned that they will not actually enjoy their inheritance. However, if you leave adequate instructions to the trustee, in the form of a Letter of Wishes, your legacy will be both safe and enjoyed.

The Letter of Wishes is non-binding on the trustee, meaning that the Trustee is not legally bound to follow the instructions. As such, the beneficiary has no legal right to compel distributions. This also means that their creditors, ex-spouses, etc. will have no legally enforceable rights. For instance, if a trust mandates that the beneficiary is to receive \$250,000 upon reaching age 25, then their creditor who wins a judgment can force such distribution to be made for their own benefit. However, if the Trustee is not legally bound to make the distribution, because it is simply a request in your Letter of Wishes, there can be no enforceable right for the creditor to exercise.

You may worry that the Trustee may disregard their intentions and not make adequate distributions to the Beneficiaries. To prevent this, I use a Trust Protector as a "watchdog" over the trust to make sure the Trustee is acting according to the client's wishes. The Trust Protector has the ability to remove and replace the trustee at any time, for any reason. The Trust Protector is given a copy of the Letter of Wishes, and will use this as guideline for when to replace the Trustee.

This arrangement is the best way of balancing the need to give the beneficiaries the benefit of their inheritance ***and*** make sure that their inheritance is never lost or taken from them by creditors, an ex-spouse, etc. The only thing left to decide is what to include in this Letter of Wishes.

This article will examine some of the common distributions provisions my clients have drafted into their Letter of Wishes. While not a complete list, this should give you an idea of what my clients like to have in their Letter of Wishes.

WHAT TO INCLUDE IN YOUR LETTER OF WISHES

My suggestion in making a Letter of Wishes is that you avoid making any distribution that would have the effect of encouraging your beneficiary to live beyond their means. One problem with inheritances is that they often artificially increase a beneficiary's lifestyle. Then the money runs out, and severe emotional and financial problems arise.

I want you to think about this concept when designing your Letter of Wishes. You do not want to make distributions that artificially increase your beneficiary's lifestyle, while at the same time depleting the trust principal, because this will eventually leave your beneficiary with an unhealthy lifestyle expectation and no inheritance to support that lifestyle.

Before we start, I want to make clear that we want to include an inflation provision in your Letter of Wishes that specifies that any figure you specify will be adjusted upwards for inflation. So if you request that a distribution of \$30,000 be made for wedding expenses, this amount will actually be larger when the time comes, as it will be adjusted upwards for inflation. This allows you to consider distributions in terms of today's dollars, rather than having to worry about what the dollar will be worth in the future.

With the foregoing in mind, let's explore some healthy distribution ideas.

Uni-Trust as the Baseline

Clients should consider establishing a base line of when distributions should be made. I like the concept of the "uni-trust" for this purpose. A uni-trust is where a trust pays the beneficiary a percentage of the trust assets on an annual basis. I almost always recommend that clients use a uni-trust if they have their Beneficiary Protection Trust™ managed by an independent trustee.

For instance, if the Letter of Wishes states that the beneficiary is to be paid 4% of the trust assets per year, and there is \$1,000,000 worth of assets on January 1st, then the beneficiary is entitled to \$40,000 that year.

I like to use the percentage of 4% or 4.5%. Assuming the assets grow at an after tax rate of 8%, there will be 3.5% or 4% of growth above and beyond the uni-trust distribution. This will allow the assets to keep up with inflation.

I also encourage clients to consider not making Uni-Trust distributions until a beneficiary reaches age 40. My logic is that a beneficiary's 20's and 30's are an important period for career and family development. An otherwise industrious beneficiary may be tempted to slack off if they are having their income substantially subsidized prior to age 40. It is my experience that once someone reaches age 40, absent particular circumstances, they are probably set in their career choice, and the uni-trust will not adversely affect them. Of course, it is important not to generalize in estate planning, and every beneficiary and family is different.

Purchase of a First Home

You might want to consider allowing a distribution in order to allow your children to purchase their first home. I recommend you limit the distribution to 20% of the purchase price as a reasonable down payment. I also suggest that you request that this distribution only be made if the beneficiary obtains the remaining 80% with a 30 year fixed loan. What we want to avoid here is making a distribution that will encourage your beneficiary to live beyond their means.

Educational Expenses

Your trust should encourage your beneficiaries to grow and enrich themselves educationally. This does not just mean college, but could also mean professional school, continuing education, and other career building instruction. It also means that distributions should be made for the purposes of your grandchildren and future generations, thus eliminating that stress for your children. Your trustee should have the authority to make distributions for 529 plans to facilitate this function.

Medical Expenses

The continuing health of your family is very important. Therefore, you should provide that reasonable distributions be made for the health care needs of your children, grandchildren and other descendants. This will take the burden of health care expenses off your family, and will allow them to live healthy lifestyles. An allowable distribution should be for health care insurance expenditures as well.

Starting a Business with a Loan

You may want to consider allowing your trustee to make a loan to your beneficiary to facilitate the start of a business. I recommend that you do this as a loan, rather than an

outright distribution, to ensure that your beneficiary knows that there are consequences to the distribution. It is my experience that gifts to start businesses are usually frivolously spent.

The business loan should be made only upon the submission to the trustee of a legitimate business plan that will have a reasonable chance of working. This will ensure that your beneficiary has a third party review of the business idea to make sure it has a reasonable chance of success.

Incentives for Attaining Educational Goals

- Grade Point Average

You could reward your child monetarily for achieving a certain grade point average in school. Obviously, this could also cause unnecessary strain in a beneficiary's life, so many clients view this as a way to influence the child to achieve a minimally expected standard, i.e. 3.0 GPA.

- Acceptance to College

You might consider rewarding your beneficiary for being accepted into a four-year university. You could make this as specific and narrow (i.e. Harvard or your alma mater) or as broad (any accredited college) as you wish.

- Completion of Grade Levels

You could reward your child for each year of college completed. This language should be drafted in a liberal fashion in order to account for the various credit standards for different colleges. You could even state that the trustee should pay for a spring break trip the next year if the previous year is completed. The possibilities here, as with all these provisions, are endless. You might want to cut this off after 5 or 6 years of school, to avoid your beneficiary becoming a professional student!

- Completion of College and/or Graduate School

You may want to give your child an added bonus upon completing a Bachelor's Degree. In addition, you may want to give an additional bonus upon the

completion of graduate school. Perhaps you also want to assign different bonuses for different GPA levels.

- **Adult Education**

You might want to allow your child to take various adult educational and professional programs such as cooking classes for enthusiast beneficiaries, or continuing education for professionals.

- **Vocational School**

Bearing in mind that your child may choose vocation school over college, you should consider including language allowing distributions to be made while the beneficiary is engaged in vocational training.

Gainful Employment

- **Distributions when gainfully employed**

You could specify that the beneficiary should be entitled to receive a set amount of dollars for every year in which the beneficiary is gainfully employed, or even that they should receive no distributions unless gainfully employed. This will give the beneficiary the incentive to both seek and retain gainful employment, and will make sure that they lead a productive life beyond simply living off their inheritance.

Gainful employment provisions should specify an age when they take effect, and should carve out exceptions, especially if you do not want distributions to be made unless there is gainful employment. Exceptions could include the beneficiary still being in school, full time caretaker, becoming disabled, etc.

What is gainful employment? The easiest standard is to ensure that the beneficiary works at least x amount of hours per week. This may also include if the beneficiary is seeking gainful employment. You should also allow the trustee ultimate discretion in the event an unusual circumstance arises.

- **Income Matching**

An alternative to simple distributions when gainfully employed is distributions that match the income generated by the beneficiary. You should be cautious here

because you may not want to provide a perverse incentive for your beneficiary to simply make as much money as possible, and lead a potentially unhappy life, just to get more distributions. This could also cause a disparity among beneficiaries, thereby causing conflict. Nor do you want to penalize a beneficiary for engaging in a low-pay, but socially rewarding profession like teaching.

To combat this, I often recommend that parents put minimums and caps on the income matching. For instance, a minimum of \$25,000 and cap of \$75,000 would mean that income is only matched for earnings above \$25,000 and less than \$75,000. This will make sure that income is matched only on gainful employment, but will not cause a huge disparity among beneficiaries.

- Stay-at-Home Parenting Provisions

One concern many parents may have, whether their beneficiary is male or female, is encouraging at least one parent to stay at home and raise the beneficiary's children. As such, you may want to include a provision giving a set amount of monthly or annual compensation to your beneficiary, or that beneficiary's spouse, should either be a stay at home parent.

- Retirement Accounts

You may want to encourage contributions to an IRA or 401k type plan through matching distributions. Obviously, if the beneficiary maxes out their contributions, these distributions would go outright to the beneficiary, rather than into the qualified plan.

- Charity and Community Contributions

For those of you who are charitably inclined, you might want to consider matching your beneficiary's charitable contributions. Are there other contributions you might want to match, such as contributions to the arts.

- Religious Pursuits

You may wish to allow your beneficiary to take distributions for religious objectives, such as sabbaticals for training, pilgrimages, etc.

Marriage

- Wedding, Honeymoon, and Wedding Expenses

You may want to specify that your child is to receive x amount of dollars in order to have a wedding. You might also want to include a monetary gift to allow the newlyweds a proper honeymoon. Do not forget to consider allowing your beneficiary to get assistance with purchasing the wedding ring.

- Marriage Counseling

It is often repeated that 50% of weddings end in divorce. To prevent this, you might want to allow your child's trust to cover the cost of marriage counseling.

Vacations

You might want to allow distributions to pay for your beneficiary and family to take a vacation every year, up to x amount of dollars.

Automobile

You might want here to allow your beneficiary funds to purchase an automobile, and the necessary funds for its upkeep. If you and your beneficiaries are classic car enthusiasts, for example, you might want provisions dealing with the ability to purchase these types of cars.

Family Bank

The Family Bank concept is gaining traction as a way of keeping beneficiaries accountable for their distributions, and forcing them to keep a productive lifestyle (in order to pay back the loans).

You need to be careful, however, in designing the Family Bank, in order to ensure that loans are not too easily given (thus discouraging repayment) nor too hard to get. You also should provide that the trustee still have discretionary power to make distributions in addition to these loans.

DISINCENTIVE PROVISIONS

You may also want to include Disincentive Provisions that ensure that distributions are *not* made in the event a beneficiary is engaging in destructive behavior.

Substance Abuse

A substance abuse provisions provides that your beneficiary will be entitled only to minimum distributions for menial care should they develop substance abuse provisions. You should include, however, a provision that allows their treatment costs to be covered, even if no other distributions are made.

Gambling Addiction

This provision prohibits distributions if the trustee learns that such distributions are going to fund a gambling addiction.

Unmarried Cohabitation

This provision would state that you want distributions withheld if your beneficiary is living with a boyfriend or girlfriend without being married.

Lack of Work Ethic

You may want to withhold distributions if your beneficiary is not working, seeking work, or going to school. This prevents beneficiaries from living an unfulfilled life by living off their inheritance.

Withhold Distributions if Affiliated with Cult

You may want to include a provision specifically withholding distributions if a family member is involved in a cult, religious order, or other organization in a manner that may cause the beneficiary to give any distributions to such organization.

If there is a provision you would like to include that you do not see in here, do not fret. Write it down, and speak with your attorney about the feasibility of including the provision in your Letter of Wishes. There are an infinite number of provisions that could be included in your Letter of Wishes. Just as everyone's family is unique, your Letter of Wishes will be unique.

I just want to encourage you to make sure that you do each provision with the idea of avoiding causing your beneficiary to become dependent on their inheritance rather than themselves. We want the inheritance to enrich your beneficiary's life, rather than support your beneficiary's lifestyle.

Other Estate Planning Documents You'll Need

In addition to your Family Protection Trust and Beneficiary Protection Trust, you will need the following estate planning documents:

- A Pour-Over Will

Upon your death, your Pour-Over Will leaves any property not transferred to your living trust before your death to your living trust. This is why it is referred to as a "Pour-Over" Will. It functions as a safety net to insure that property owned in your individual name rather than in the name of your living trust is ultimately managed by your successor Trustees as provided in your living trust. This is a second best case scenario, though. Your goal is to avoid probate altogether by transferring all of your assets to your living trust during your life. Your will is merely a backup document that ensures that all your assets are ultimately controlled by your living trust.

Your Pour-Over Will shall contain executors that you choose to manage your probate estate in front of the probate court. These persons, called Personal Representatives or Executors, will hire an attorney to help them in the process, but will ultimately be responsible for overseeing and managing your affairs in Probate.

Your Pour-Over Will also includes your nominations for guardian should both you and your spouse die.

- A Power of Attorney

Your estate plan should also include a Durable Power of Attorney for property management. In this document, you appoint an agent to act for you if you become disabled. Your agent is authorized to transfer property to your living trust, to make withdrawals from your retirement assets, or to do anything else that you want your agents to do for you to take care of you in the event that you become unable to effectively manage your property or financial affairs.

Your power of attorney will also contain a nomination of a conservator for your person or estate. In addition, your power of attorney will include a nomination for guardian of your children should you become incapacitated.

- A Certification of Trust

When you transact business on behalf of your living trust, you will sometimes be asked to produce a copy of your living trust document. Financial institutions and others who deal with you will want proof that your living trust exists, that they are dealing with the true trustee, and that your living trust gives your trustee the power to do what your trustee proposes to do.

If your living trust includes personal or financial information that you want to keep private, most financial institutions will allow you to substitute an “affidavit” or “declaration” or “certification” of trust – a document that contains only the provisions that the financial institutions or others need to see. We refer to these documents as a “certification of trust.”

In addition to a statement that your living trust is valid, a certification of trust may include copies of key pages of your living trust as attachments. Normally these pages will confirm the following:

- The identity of the current and successor trustees of your living trust;
 - The authority and powers that the living trust grants to the trustees; and
 - The signatures required by the living trust agreement.
- An Assignment of Personal Property to Trust

An Assignment of Personal Property is a document that transfers your personal property, including cars, furniture, art, etc., to your Family Protection Trust.

- Advanced Health Care Directive

Your Advance Healthcare Directive authorizes your agent to make medical decisions for you if you cannot express your wishes or make the decisions yourself. In addition, your Advance Healthcare Directive authorizes your agent to obtain copies of your medical records. You may revoke your Advance Healthcare Directive at any time by informing your agent, in writing, that you are revoking the appointment. You should also send a copy of the written revocation to anyone who has a copy of the original Advance Healthcare Directive.

- An Authorization for Release of Protected Health Information under the Health Insurance Portability and Accountability Act (aka HIPPA Authorization)

Your Authorization for Release of Protected Health Information is a document required by the Health Insurance Portability and Accountability

Act (“HIPAA”). This document allows the identified persons to obtain protected health information on your behalf in order to make informed decisions about your care and the payment of medical bills.

- A Living Will

Your Living Will serves to inform your doctors that you do not want extraordinary medical measures taken, especially those that would cause you pain or discomfort, if those measures would only prolong the dying process. This document backs up your Advance Healthcare Directive. Anyone can deliver this document to your doctors if your agent under your Advance Healthcare Directive is unavailable to make health care decisions for you.

- Memorial Instructions

During a period of your disability or in the event of your death, your loved ones are often not able to think clearly. Some decision must be made within hours of death. Any help you can provide will be most appreciated. This section allows you to provide important information to your family and loved ones.

You may want to include your burial or cremation wishes and a description of the kind of memorial service you would like. You may also desire to express your feelings about the general amounts that should be spent for these remembrances. Or you may have made pre-arrangements that should be described.

You may want to do this by completing the accompanying forms or you may want to leave a personal *memorial letter*. In either event you should consider including the following information: religious affiliations, pre-purchased plans, desire for private service or service for friends and relatives, pall bearers, viewing wishes (open or closed), scripture readings, music selections, etc.

- A Property Agreement (for married couples)

For married couples, it is often a good idea to sign a Community Property Agreement. This document makes it clear that any property covered by the Agreement is to be considered Community Property with Right of Survivorship. This will allow for a 100% step-up in tax basis of such property upon the death of the first spouse. This will provide an excellent tax benefit to the surviving spouse. However, be careful, and property you list as Community Property will be considered Community Property in the event of a Divorce.

Planning for Large IRAs and 401Ks

There is a coming disaster awaiting those beneficiaries who will be inheriting the \$3 trillion plus dollars currently sitting in IRA and 401k accounts. The problem is twofold. First, the “triple-tax” awaits those who inherit IRAs and 401ks and can eat up to 70% or more of an inherited IRA. Second, even if you minimize the triple-tax through a “Stretch,” a problem awaits in that IRAs are an extremely attractive asset for beneficiaries’ creditors, ex-spouses, and lawsuit plaintiffs.

The purpose of this article will be to (1) explain the triple-tax and its effects, (2) how to “Stretch” an IRA to produce millions of dollars of distributions to your family while minimizing the triple-tax, (3) explain why stretching will generally not work, and (4) explain how a Stretch IRA Trust can force the “Stretch-out” to occur.

At the end of this article, you will be equipped with the knowledge necessary to defuse the coming IRA time bomb and create an explosion of benefits for your loved ones. You will also be armed with an action plan of steps needed to ensure the stretch occurs. For the purposes of this article, please note that I use the term IRA to generically refer to any qualified retirement plan, such as a 401k, 403b, etc.

Part I: Triple-Tax

An IRA is subject to three taxes upon your death. These taxes are (1) the federal estate tax, (2) the federal income tax, and (3) state income taxes. This section will explain how these taxes act as a deadly combination that will decimate your IRA or 401k.

Federal Estate Taxes

The federal estate tax is a tax due upon the death of an individual or the surviving spouse (in the case of a married couple). Each individual is allotted an estate-tax credit equal to the applicable amount in the year of death. Married couples get one credit per spouse; however, at least one credit is often lost due to poor planning and lack of a properly drafted revocable living trust.

For every dollar’s worth of assets you have above the applicable credit amount, you will lose a portion of your estate to an estate tax, at rates determined by the Internal Revenue Code. The exclusion amounts and the highest estate tax rates are changing over the next few years.

The estate tax credit amount is increasing, until 2010, when there is no estate tax.

Year	Exemption Amount	Highest Tax Rate
2007	\$2,000,000	45%
2008	\$2,000,000	45%
2009	\$3,500,000	45%
2010	Unlimited	n/a
2011	\$1,000,000	55%

However, this reprieve is only temporary and will end in 2011, when the credit decreases to \$1,000,000. Any amount owned above this threshold will be subject to taxes as high as 55%.

Example #1

Bob, age 65, has \$1,000,000 in real estate property, \$500,000 in liquid business, and a \$500,000 IRA. If he were to die between 2007 through 2010, there would be no estate tax due, because his assets fall under the credit exemption amount. But say Bob dies in 2011, at age 69. According to present law, suddenly Bob's house meets the credit exemption amount. This means that the entire IRA is subject to an estate tax as high as 55%. Assuming growth of 8%, the IRA There will also be estate taxes due on the business, but let us ignore those for the purposes of this article and focus solely on the IRA estate taxes.

Federal Income Taxes

In addition to any estate taxes due, your IRA will be subject to federal income tax. This tax is currently at rates as high as 35%. In addition, any amounts distributed to pay estate tax are subject to federal income tax. So in the example above, if Bob's heirs pay the IRA estate tax bill of \$420,913 by taking a distribution from the IRA, then there will be a deemed distribution of \$420,913, subject to a tax of 35% equating to \$147,319. That means \$147,319 in addition to the \$420,913 estate tax.

State Income Taxes

Finally, Bob has state income taxes due in addition to the federal estate and income taxes. The California rate is as high as 9.3%. When that \$420,913 is used to pay the estate tax

bill, California gets \$39,145, in addition to all other taxes paid.

Triple-Tax Recap

As you now see, the triple-tax can really crush an IRA. In our example, Bob's decedents had to pay (1) \$420,913 in federal estate taxes, (2) \$147,319 in federal income taxes, and (3) \$39,145 in state income taxes. That's \$396,825 in potential taxes, totaling 79% of the IRA. The result is even worse if Bob's beneficiaries withdraw the entire IRA, as will be discussed below. Now, with some crafty accounting and deductions, an experienced CPA can reduce the income taxes, somewhat, by deducting the state income taxes paid from the federal. However, the end result is still combined taxes of over 70%. This is the worst result possible, and we need a plan to avoid it.

Part II: "Stretching" an IRA

Do not get discouraged at this point. You can not only beat the triple-tax, but you can turn your IRA into the best possible asset for your loved ones to inherit. There are two steps to beating the triple-tax.

Step One: Estate Tax Paid with Other Assets

First, we must make sure that any estate taxes are paid with non-IRA assets. In Bob's case, he had two other assets—real estate and a business. If possible, any estate taxes should be paid with these assets. However, often these assets are not liquid enough to produce the cash necessary to pay estate taxes. If this is the case, Bob should have a life insurance policy, owned by an Irrevocable Life Insurance Trust, with a payout large enough to cover potential estate taxes. If Bob can avoid having his beneficiaries be forced to use IRA assets to pay estate taxes, then no distribution is required (if the "Stretch" requirements are met), and thus no income taxes are due as a result of the payment of estate taxes. By providing liquid funds to pay estate taxes and coordinating the entire estate plan (including the Revocable Living Trust) with the IRA plan, Bob can avoid incurring unnecessary income taxes. In addition, the Life Insurance Trust will cover all estate taxes and ensure that Bob's loved ones get the full benefit of his estate without being reduced by estate taxes. Then Bob's children will have the ability to "Stretch" the IRA and thereby minimize the income tax portion of the time bomb.

Step Two: Stretch the IRA

"Stretching" an IRA is when the beneficiaries of an inherited IRA take only the required

minimum distribution, as determined by such beneficiary's age, rather than the original IRA owner's age. Stretching is a very new concept and has only been around a few years. In fact, the concept is so new that a majority of estate planners are not sufficiently trained to handle IRA planning.

Let us step back and explain this by looking at how to handle distributions from your IRA. You may take distributions without early withdrawal penalties at any time after age 59 ½. However, most people use other assets, seeking to avoid the ordinary income tax treatment of their IRA assets. When you reach age 70 ½, however, you will be required to begin taking required minimum distributions (RMDs), unless you have a Roth IRA, in which case, no RMDs are required during your lifetime. These distributions are taxed at ordinary income tax rates (subject to some allowances) when they are withdrawn (unless your IRA is a Roth IRA), and everything remaining in the IRA is not subject to tax. As such, taking only the RMD will allow you to accumulate much more wealth within your IRA, all growing tax-free. You calculate your RMD by dividing your account balance as of December 31 of the previous year by your distribution factor, found in the Uniform Life Tables published by the IRS.

Example #2

Bob turns 74 and his IRA was \$500,000 on December 31 of the year before; therefore, he must withdraw \$21,008.40. The amount necessary to withdraw will increase steadily during his remaining years. If Bob lives until age 80 and takes only the RMD every year, he will receive \$210,912.06 in total distributions from his IRA.

An interesting thing happens if you only withdraw the RMD. Because the tax code wants to make sure you do not outlive your IRA, they make the RMDs small enough so that your IRA will last well into your 100s. This means that, in reality, your IRA account balance will be greater when you die than when you begin taking required minimum distributions. This fact makes planning for your IRA even more important.

Example #3

If Bob dies at 80, his IRA will be worth \$765,298.16, assuming 12% growth. In fact, Bob's IRA will not start declining in value until he is 97 years old, when it will be worth \$1,427,830.71. In fact, Bob would have to live until age 115 for his IRA to fall under the original \$500,000 value. Given that the average American does not live past 85, you can see that, most likely, an IRA will be larger at death than when RMDs are first taken out.

This is all due to the wonders of tax-free compounding. Please feel free to test these results on the Stretch IRA calculator found at:

<http://www.principaltrust.com/tools/calculators/stretchira.htm>.

When a beneficiary inherits an IRA, these wonders of tax-free compounding compound (no pun intended) to produce even more incredible results. A beneficiary inheriting an IRA can take distributions according to their age on what is called the “Single Life Table” produced by the IRS. The distribution factors for younger beneficiaries are much lower than that of the original IRA holder, and as such, the RMDs are lower, and more can be allowed to accumulate tax-free within the IRA itself. The results are astounding, but show why Albert Einstein called compound interest the 8th World Wonder. Say Bob’s son, Jack, inherits his father’s IRA when Bob dies at age 80, when Jack is age 50. If Jack lives until age 80 as well, he will receive \$7,299,862.71 dollars of distributions over his lifetime. In addition, when Jack dies, there will still be \$3,146,894.13 in the IRA. Now, Jack’s children cannot “Stretch” the IRA but instead will receive the remainder over the next 4 years (there will be a little growth, meaning \$3,495,571.10 in total distributions to Jack’s children). All in all, the total family wealth created by this is \$10,895,441.81 in distributions after Bob’s death. Now, these distributions will be taxed; however, the fact that only the RMD is taxed and the rest allowed to grow tax-free creates this amazing amount of wealth.

Recap of the Stretch

Take a look at the alternatives. Bob can have 70% or more of his IRA lost immediately to federal estate, federal income, and state income taxes. In our example, if he died at 80, there would be \$765,298.16 left in the account. The federal estate and federal and state income taxes will total around \$607,378.88. That’s 77.5% of the inherited IRA! Jack would receive just \$171,620 in distributions (assuming he just took out what was left and Stretched the remainder. Alternatively, Bob can plan for the Stretch, have Jack receive \$7,299,862 of distributions over his lifetime, and has almost \$3,500,000 left over for his grandchildren.

The contrast is obvious, and the course of action is clear. Your IRA can either be your children’s worst tax nightmare, or the greatest source for generational wealth. In order provide the most benefit possible from your IRA, you **MUST** take the steps necessary to make the Stretch happen. However, as we will see, the Stretch is neither automatic nor is it likely to happen without planning on your part.

Part III: WARNING: Stretching is Neither Automatic Nor Likely

Please note that the awesome power of the Stretch is not automatic, and most people who inherit IRAs will never experience its power. The problem is that the Stretch will only occur if your beneficiary withdraws no more each year than the RMD. If the beneficiary withdraws more than the RMD, the tax deferral is lost, and they will owe a large tax bill on the amounts withdrawn. When the Stretch-out is lost, we call this a “Blow-Out.”

Reasons for Blow-Outs

Even if you avoid the problem outlined above of being forced to use IRA assets to pay estate tax, it is still very likely that your beneficiary will withdraw the IRA within one year after your death and be forced to pay estate taxes. Why would they do this? Why would they throw away millions of dollars of wealth and suffer a Blow-Out? This is something you really need to worry about.

The reasons are numerous, but I will try to list the most common reasons here:

1. Not understanding the rules and choices. Most beneficiaries, when they learn they have inherited an IRA, will not know about the Stretch and will just ask for the check from the administrator. Once this happens, the cat is out of the bag, and there is no way that the Blow-Out can be corrected.
2. Asking the advice of the custodian. Often when beneficiaries contact an IRA custodian and ask what their next step should be, the custodian just sends them the check, thereby blowing the Stretch.
3. Corporate plans require distribution within 1 year. While less frequent, some corporate plans (i.e., 401ks and 403b plans) require distributions to be made within one year of the deceased participant’s death. This causes the beneficiary to withdraw the amounts in the account, thereby blowing the Stretch.
4. Beneficiary does a rollover. Non-spouse beneficiaries are not allowed to “rollover” an inherited IRA. This will be deemed a distribution and thus a Blow-Out. However, often beneficiaries are not aware of this, fail to seek advice, and ruin their chances of a Stretch.
5. Beneficiary wants to spend it. The average inheritance, when received by a beneficiary, is completely consumed within one year. IRAs are not immune to this problem. But IRAs are even worse than regular assets. If your beneficiary spends a

normal inheritance, the money is gone, and that's that. With an IRA, not only would the money be gone, but there will be a huge tax bill to pay.

As you can see, for the above reasons, it is quite unlikely that the Stretch will occur. But what if your beneficiary is both wise and prudent? What if they (1) learn the Stretch rules and (2) have the discipline necessary to take only the RMD, and no more, every year. There still are a plethora of problems that can cause a Blow-Out.

Creditors, Predators, and Divorce

One of worst problems facing inherited IRAs is the lack of creditor protection. If you leave your IRA outright to a beneficiary, then there is a good chance they will eventually lose some or all of the inherited IRA to one of the following:

Creditors. If your beneficiary is in debt and cannot pay, then their creditors can go after their inheritance if distributed outright to your beneficiary. This has become even easier with the Bankruptcy Act of 2005.

Divorce. In a perverse twist, tax laws actually make an IRA an excellent asset for a divorcing spouse to try to take, because the distribution will be taxed to your beneficiary, while their ex-spouse gets the proceeds tax-free. If your child is married, then this is a huge problem, considering 50% of all marriages end in divorce. You can be sure that if your beneficiary gets divorced, their ex-spouse's attorney will fight furiously to make sure their client gets the IRA.

Lawsuits (a.k.a., "Litigation Lottery"). A new lawsuit is filed every 90 seconds in California. I imagine that in a few years the most common source of workplace repetitive stress syndrome will come from court clerks furiously stamping the latest lawsuit. An inherited IRA does not receive the same level of creditor protection as it does in your hands. As such, your beneficiary could lose their IRA to any number of lawsuits, whether legitimate or frivolous.

You must think by now that the situation is hopeless. You see the power of the stretch but are sure that your loved ones will never enjoy the benefits due to the roadblocks in the way. Well, they can, if you help them. The choice is yours. How can you ensure that your beneficiaries enjoy the Stretch-out? Let's find out.

A Living Trust Won't Work

You may think that you will successfully avoid the Blow-Out by simply leaving your

IRA to your Living Trust. While Living Trusts are great for avoiding probate and can have other benefits (if properly drafted), they are generally not good recipients of IRAs for the following reasons:

Usually Limited Creditor Protection. If properly drafted, a Living Trust can provide the most asset protection possible to your family. However, 90% of all Living Trusts do not contain the language necessary to ensure this asset protection. As such, your Living Trust would probably not protect your beneficiaries from creditors, divorce, and lawsuits.

Mandatory Distributions. Most Living Trusts contain a provision that states that all assets must be distributed to the beneficiaries immediately or upon the beneficiary reaching a certain age. If this is the case, such distribution makes the IRA proceeds immediately taxable.

Oldest Beneficiary is Spouse. When an IRA is payable to a trust, without special planning, the life expectancy used in taking RMDs is the oldest beneficiary. For married couples, this is usually the surviving spouse. As such, the children will not be able to take RMDs according to their life expectancy, but instead according to that of the surviving spouse, resulting in accelerated distributions and a Blow-Out.

Non-Designated Beneficiaries. For a Stretch to occur, all beneficiaries must be individuals. If your trust leaves anything to a charity or other non-individual beneficiary, the Stretch cannot occur, and you will incur a Blow-Out.

No Stretch Language. A Standard Revocable Living Trust does not contain the language necessary to allow the trustee to take only the RMD according to a beneficiary's age. As such, the trustee will probably not be allowed to Stretch an IRA with most trusts.

As you can see, for a variety of reasons, a Revocable Living Trust is not the answer and will in fact make absolutely sure that the Stretch does not happen. The only way to ensure that the Stretch will occur and that your beneficiaries avoid losing their inherited IRA to the IRS and/or creditors is by using a Stand-Alone Stretch IRA Trust.

Part IV: The Stand-Alone Stretch IRA Trust

If you wish to both ensure that your beneficiaries are able to take the Stretch-out and provide them with asset protection to avoid losing their inherited IRA then a Stand-Alone Stretch IRA Trust is the only logical solution.

The Basics

The Stand-Alone Stretch IRA Trust is a Revocable Trust that you establish for the express purpose of being the beneficiary your IRA upon the death of you and your spouse. This trust is completely separate from your main Revocable Living Trust, which is meant to own non-IRA type assets.

Unlike your Revocable Living Trust, the Stand-Alone IRA Trust is specially designed to be the beneficiary of your IRA upon your death. It contains special language that allows the trustee to withdraw the RMD according to your beneficiary's age, thus preserving the Stretch. However, the main advantage is that your beneficiary will never be able to take out more than the RMD, unless the trustee deems such distribution necessary. This will force the Stretch and ensure your family receives as much as possible from your IRA.

The choice of trustee is important with a Stretch IRA trust. Obviously, having your beneficiary serve as trustee defeats the purpose. A beneficiary serving as trustee could just choose to withdraw more than the RMD for themselves, thereby causing a Blow-Out. Instead, I recommend that clients choose a corporate trustee to serve as the fiduciary of their Stretch IRA Trust. A corporate trustee is an entity, such as a bank or other financial institution, which will serve as an independent fiduciary acting in the interests of your beneficiary. This serves the purpose of forcing your beneficiaries to take only the RMD every year, thus ensuring they will receive the most benefit possible from your IRA.

Another benefit of an independent corporate trustee is asset protection. A Stretch IRA Trust, combined with an independent trustee will ensure that your beneficiary will receive the full benefit of their trust, despite creditors, divorce, lawsuits, or other attempts by a third party to take your IRA.

This asset protection is strengthened by the fact that your trustee is not required to distribute the RMDs every year to your beneficiary but may instead choose to accumulate such RMDs within the trust, should the beneficiary run into creditor problems. This "accumulation" will give the beneficiary the ability to settle with their query on favorable terms, instead of being forced by a court to hand over the IRA to their creditor.

Each Beneficiary May Take RMDs According to Their Age

Normally, when a trust is the beneficiary of an IRA, the RMDs will be made according to the age of the oldest beneficiary. In the case of a normal Living Trust, that beneficiary is the surviving spouse, who is significantly older than the children. Having RMDs taken at

the spouse's age defeats the purpose of the Stretch and causes a Blow-Out. Instead, the beneficiaries of your Stand-Alone IRA Trust should be your children, grandchildren, or other significantly younger beneficiaries. As will be explained below, your spouse will still be able to benefit from your IRA, but they will not be a beneficiary of the Stand-Alone IRA Trust.

Another recent development is an IRS ruling stating that with proper planning, your Stretch IRA Trust can use the life expectancy of each beneficiary for their portion of the IRA. This is done by including language in the trust separating the inherited IRA into Separate Share Trusts for each beneficiary. This means every beneficiary's share is separate, and distributions to one beneficiary do not affect another beneficiary.

In order for this Separate Share treatment to occur, you must properly list each beneficiary's separate share trust on your IRA custodian's Beneficiary Designation Form. This language is critical and should only be drafted by an attorney who is an expert in this area.

But What About Your Spouse?

You may have been thinking that this idea is great, but what about my spouse? The answer is that your spouse can still enjoy your IRA after your death. In fact, your spouse will be able to "Stretch" your IRA according to his or her age by "rolling-over" your IRA after your death. Once that rollover is done, your spouse will just list your trust as the designated beneficiary, allowing the Stretch to occur after his or her death. Due to the tax-free compounding of your IRA when inherited by your spouse, your IRA will likely be larger after your spouse's death than when he or she first inherits it

Example# 4

Let's go back to our example with Bob, only this time we will broaden the facts a little. Bob, currently 74, is married to Sue, who is 68. Bob's IRA is now worth \$500,000. Bob decides to set up a Stretch IRA Trust, with Jack as beneficiary. Bob fills out his Beneficiary Designation Form, naming Sue as the primary beneficiary and Jack's separate Share Trust as a contingent.

As stated before, Bob then dies at age 80, when the IRA is worth \$765,298.16. Sue immediately rolls-over the IRA and begins taking distributions according to her age. She names Bob's Stretch IRA Trust as her beneficiary. She lives until age 80, taking out \$287,576.00 in RMDs. At her death, the IRA is worth \$1,236,006.24. The trustee of the

trust then begins taking distributions according to Jack's age. These RMDs will total \$10,284,151.95, assuming Jack dies at age 85.

Now assume that sometime after his father and mother's death, Jack is the subject of a lawsuit and owes \$2 million. Without the Stretch IRA Trust, he could lose his inherited IRA to satisfy the judgment. With the Stretch IRA Trust, however, the IRA is safe, and he will have strong leverage to settle the judgment on favorable terms.

CONCLUSION

As you can see, your IRA can be the best asset your children inherit, or the worst. You can have over 70% lost to taxes and the rest subject to creditors, divorce, and lawsuits, or you can do preemptive planning to protect your family and help them enjoy millions of dollars from your IRA.

Stretching an IRA will both minimize your loved ones' tax burdens while at the same time providing potentially millions of dollars of wealth to several generations. However, as we have seen, the Stretch will generally not happen on its own. Mistakes or frivolous spending can cause a Blow-Out and cause huge tax consequences. In addition, creditors, ex-spouses, and lawsuits can further decimate an inherited IRA.

The beauty of the Stretch IRA Trust is that it puts the Stretch on autopilot, forcing it to occur, while at the same time preventing the wrong parties from taking the IRA from your beneficiaries. Really, the decision to do a Stretch IRA Trust is a "no-brainer." The set up fees are small compared to the benefit your loved ones will receive.

A Stretch IRA Trust will ensure that your IRA serves as an enduring legacy, rather than a problem asset. The good news is that the choice is up to you. If you take the step of having a Stretch IRA Trust drafted, then you will have ensured the protection of your family for years to come.

Guardianships: An Overview

An often overlooked and neglected part of the estate planning process is the choice of a guardian for your minor children. This is often the most difficult part of planning your affairs, and is often agonized over by my clients. This is essential to your family's security, however, it should be thoroughly thought out with the assistance of a qualified estate-planning attorney. Appointing a guardian allows you the opportunity to make a tremendous positive impact in your child's life, should something happen to you.

The decision of who will be your child's guardian is vital in protecting your family. However, most people do not consider the full scope of the choices inherent in picking a guardian. For instance, most people just write in a guardian to take care of their kids in the event of death. However, a choice of guardian deals with more than what happens if you die. In fact, there are three separate instances when a guardian may be required, and each may require a different set of guardian choices. These three instances are:

1. What Happens If You Die?
2. What Happens If You Are Incapacitated?
3. What Happens If A Temporary Emergency Arises?

This article will examine these three occurrences in depth in an effort to help you make the important choice of who will take care of your children if you cannot. First we will examine what rights you have in California regarding choosing a guardian for your children. Next we will examine each of the above scenarios, in an effort to help you choose an appropriate guardian for your children.

How Do You Select a Guardian?

California Probate Code § 1500 allows the parent of a child to nominate a guardian. In order for this nomination to be legitimate, the other parent of the child must either (1) agree to the same guardian; or (2) be dead or otherwise lack the capacity to choose an alternate guardian. As such, I have my clients choose the same guardians, in the same document, with each party signing the document, which is called a Guardianship Nomination.

Traditionally, the parents will name guardians for their minor children in their will. However, this raises two problems, given that (1) a will generally is only used after the parent dies; and (2) the most frequent need for a guardian arises from incapacity. This

being the case, it is preferable, in my opinion, to use a single Guardianship Nomination that deals with all three of the instances described above.

The proper form of a Guardianship Nomination is interesting. Post death guardianship nominations made by will, require the formalities of a will, which includes having the will witnessed by two non-interested parties. Incapacity nominations are traditionally made in a Durable Power of Attorney, which requires a notarization. This being the case, I draft my client's Guardianship Nomination Document to be a hybrid of a will and durable power of attorney, requiring both witness and a notarization.

Another issue with nominating a minor is the person who can actually do the nominating. The probate code specifically names a "parent" as the only person having that right. As such, the parent cannot leave the duty of nominating a guardian to a person or series of persons. However, an exception arises for adoptive parents. As such, a request should be put in your guardianship parents requesting that your guardian adopt your child if you would like to leave the naming of successor guardians to that person.

Who Should Be Your Guardian?

The probate court will name your child's guardian on a permanent basis, taking into account your instructions on your Guardianship Nomination. This begs the question, who should this person be? Well, there are about a million factors that should go into choosing your guardian, and each situation is unique, but here are some ideas that will help you choose an appropriate guardian should you die.

1. Maturity. Is this person mature enough to take care of your child? In addition, do you want to name older siblings as a guardian for their younger siblings if they reach a certain age.
2. Patience. Is this person patient? Are they used to having children around? Will they be able to handle your children for an extended period of time?
3. Age. Consider whether your proposed guardian is too old or has too little stamina to take on the challenge of your children.
4. Presence of other children in the home. This is a double-edged sword, and should be considered carefully. On one hand, you might like that your guardian has other children with whom your children are comfortable. On the other hand, is this proposed guardian dealing with too much to add your kids to their home?

5. **Trust and Integrity.** Remember that your guardian will likely have a huge impact on the emotional development of your children. As such, you should consider their ethical nature, because it will be passed on to your children.
6. **Religion or Spirituality.** Do you want your children to continue to be raised in a certain religion or church after you are gone? If so, consider someone with your same belief system.
7. **Stability.** Will your proposed guardian provide a stable home for your children? Alternatively, are they on the verge of divorce every other weekend?
8. **Willingness to Serve.** Above all, are they willing to serve? You should ask them this, and require that they consent to your selection.
9. **Location, Location, Location.** Where will your child live when you are gone? As we will see below, this may be more of an issue if you are just incapacitated or a temporary emergency arises. Nonetheless, do you want your child to go to the same school, keep the same friends, etc. in an effort to maintain normalcy? If so, you must name a guardian in the same area as your current location.

There are several types of people my clients often choose to serve as guardians. These people typically include:

1. **Relatives.** Your parents, siblings, cousins, etc. are excellent choices for a guardian.
2. **Your Other Children.** Your younger children's older siblings can be good choices. You may want to stipulate that they must reach a certain age before serving. In any event, they must be over the age of 18.
3. **Friends.** Your friends may be excellent choices, especially for Disability Guardians, given that they live in the same area as you. What about long-time friends you got to know at parenting functions? They make excellent choices, because you know their parenting philosophy.
4. **Business Partners.** You may admire your business partners for their work-ethic, determination, etc, and want them to pass these values onto your children.

5. Church Members. If you attend a particular church, you might want fellow church members to serve as your guardian, to participate in your children's religious upbringing. Or, you may want to request that this person take your child to church every Sunday, even if they live with another person.

How many guardians should you choose? I say as many as possible, each stepping in line if the previous guardian cannot serve. I encourage you to write down every person whom you would rather see your child go with than go to foster care. You never know how many of your choices will be unable or unwilling to serve as guardian, and as such, you must name as many as possible, in the order of fitness to serve.

You do not necessarily need to consider the financial ability of your guardian to manage your children. You can provide extra sources of funds for your children through life insurance and your assets, and can have these funds managed by a third party for the benefit of your children. I say third party not because I do not trust your guardian to manage the funds, but to prevent the inherent conflict of interest that arises when the same person manages your child and their inheritance.

What Happens if You Die?

The first, but thankfully least common, instance that requires a guardian for your minor children is the instance of your death. In the event of your death, a properly drafted Guardianship Nomination will allow the probate court to name your choice as permanent guardian. However, as you may be well aware, the probate court moves very, very slowly. As such, limiting your guardianship nomination to a permanent guardian named in a will is very detrimental to your children, due to the long time between when you die and when their permanent guardian is approved.

The solution to the long probate process is to make sure you name a temporary guardian in your Guardianship Nomination. A temporary guardianship is a quick probate proceeding that will allow the court to name someone for your children to stay with until the permanent guardianship is sorted out.

As you can see, the choice of nominating a guardian after you are gone must take many factors into account. Naming a guardian in the event of your incapacity or a temporary emergency must take these factors into account as well, but as we shall see there are additional factors to consider.

What Happens If You Are Incapacitated?

You are six times more likely to become incapacitated than die in any given year. As such, serious thought should be given to what happens if you are temporarily or permanently disabled. The factors listed above will still be important in choosing guardians in this instance. However, some factors will take on greater importance.

The most important factor to consider in choosing a Disability Guardian for your children is probably location. If you are incapacitated, you will probably not want your children to move to a distant relative in the East Coast because (1) they will not be able to see you in the hospital or other care facility; (2) they will not be able to continue with their normal day to day activities; and (3) financial issues may arise if you have a third party trustee taking care of both you and your children, and you are in different locations.

As such, I tend to encourage clients to choose trustees who live in the same area. You should try to provide as much continuity as possible for your children in stressful times, and staying the same location will help do this. To facilitate this, you may even consider allowing an out of town resident to come live in your home with your children, as this may make it easier for them to accept guardianship duties.

What Happens If A Temporary Emergency Arises?

If an emergency arises, there will be a lapse of time until your permanent guardian is approved by the court. However, we want to avoid, if possible, a situation where children's protective services places your child in foster care pending court approval. Foster care is a troubled system, and is no place for your child if it can be avoided.

To combat this problem, my Guardianship Nomination selects temporary guardians to act in the event an emergency would otherwise leave the fate of your child up to children's protective services. This is designed to avoid foster care, and place your children with familiar faces in a safe environment.

Often your Temporary Guardians will be the same as your Disability Guardians. However, in some circumstances, such as when your Disability Guardian is not local, you may want to name an alternate. In addition, you may want to name a number of Temporary Guardians in case your first choice is on vacation, sick, etc.

Conclusion

The selection of a guardian for your minor is a unique, personal choice. It is often the most important part of your estate plan, yet it is generally overlooked and under considered. Please take the time to consider this carefully, as this might be the most important selection you make in your Estate Plan.

25 Mistakes Successful Families Make with Estate Plans

It is my sincere belief that affluent clients, especially those with a net worth between \$1million and \$15 million, are horribly underserved by estate planning attorneys. On one-hand, there are “trust-mill” type firms that just take-in and spit-out clients with cookie-cutter Living Trusts at an alarming rate for rock bottom prices. On the other, there are large firms in pricey office spaces, whose target clientele is the ultra-rich, often charge tens of thousands of dollars for even their simple, foundational estate planning.

How do you know whether your estate plan is right for you and your family? The key is hiring an attorney who seeks to understand your family’s unique needs and incorporate those needs into estate planning documents that will protect your family, all at a fair price that is less than the value it provides to you and your family.

MISTAKE #1. Assuming Your Estate Plan Should Include a Living Trust.

In all likelihood, your estate plan should include a Revocable Living Trust. However, your attorney should explain to you first the pros and cons of the Probate Process. This will allow you to weigh the benefits of a Living Trust so you can make an informed decision about whether one is right for you. In my experience, there are a great deal of people out there who would be better off with nothing at all as opposed to their current Living Trust.

MISTAKE #2. Assuming all Living Trusts are the Same.

Once you’ve made a decision to protect your family with a Living Trust, it’s easy to assume that any Living Trust will do. However, this is not the case. I know this because I review dozens of existing Living Trusts for clients each year. In fact, I have a 12 point analysis I’ve developed to show clients where their existing Living Trust is deficient. I have yet to review a Revocable Living Trust that meets even *half* of these requirements.

MISTAKE #3. Assuming that a Living Trust is the same as an Estate Plan.

One common misperception I’ve seen is the assumption that having a Living Trust is the same as having an Estate Plan. Nothing could be further from the truth. A Living Trust is simply one part of an overall estate plan designed to allow you to control your wealth and protect your family. There are several issues, such as IRAs and 401Ks, Asset Protection, and Estate Taxes, that are not adequately addressed by a Living Trust. Likely, more planning is essential for complete protection of your family and your wealth.

MISTAKE #4. Assuming that all Lawyers are the Same.

A common mistake is to assume that any Lawyer can do your Estate Plan. This is not the case. Many Lawyers are the proverbial “Jack-of-all-Trades and Master of None”. They do a little divorce law, a little criminal law, and a little estate planning. As a result, they are not well versed in the complexities of estate planning. Your attorney, to be effective, should earn at least 75% of his or her revenues from estate planning.

MISTAKE #5. Assuming that a Low Cost Trust Mill Can Handle Your Estate Plan

A Trust Mill is a law firm that churns out dozens of cookie-cutter Living Trusts every month, often for extremely low prices under \$1,500. These documents are all the same, only the names change. The result is that your unique family needs are not incorporated into your estate plan. Think about it. What are they leaving out of your estate plan that allows them to charge such a low rate?

These may be fine for young families still acquiring assets, but if you have a net worth of above \$1,000,000, these plans can equal disaster for you and your family. Instead, you need a customized plan that involves (1) a substantial discussion with your attorney about the specific needs of your family and (2) customized legal documents that encapsulate that counseling session.

MISTAKE #6. Paying High Costs of a Large Law Firm.

With the above statement that it does not make sense for affluent clients to seek the assistance of a trust mill to prepare your estate plan, you may think the only other alternative is to seek the assistance of a large, high-price law firm.

Choosing a large law firm has many problems. First, they are extremely expensive. Living Trusts at these firms often start at over \$10,000, with advanced estate planning often costing between \$100,000 and \$250,000. While this may make sense for families with a net worth in excess of \$10 million, it does not make sense for the majority of affluent Americans.

In addition, the little known secret about big firm estate planning is that the so-called “Estate Planner” in the firm is often actually a Corporate Tax Attorney who normally deals with Mergers and Acquisition, and just happens to dabble in estate planning for corporate executives. This means you may pay a great deal for an estate plan that is not even prepared by a knowledgeable estate planning attorney!

Instead, you need to have an estate planning attorney who focuses on Affluent Clients with \$1million to \$10 million. Affluent clients with a net worth in this range have a

different set of needs that aren't addressed by either trust mills or large, expensive law firms. Unfortunately, there are not many attorneys who focus on clients in this range, and who have developed a unique set of skills necessary to meet the needs of these clients.

MISTAKE #7. Assuming Your Living Trust Will Avoid Probate.

The most commonly used technique used to sell Living Trusts is the idea that they "Avoid Probate". However, a Living Trust is worthless until it is "funded", meaning that title to assets you own are transferred to the trust. Most attorneys do not assist clients with transferring assets to their client's trusts. In order for you to be sure that your trust is funded correctly, you should choose an attorney who will not only help you fund your trust, but guarantee that it will be funded.

MISTAKE #8. Choosing "Probate-Avoidance Plan" form of Estate Planning.

The standard for estate planning attorneys is the "Probate Avoidance Plan". Many attorneys will only talk to their clients about the "Living Trust". However, for many affluent clients, there are many other considerations that come into play, for example, dealing with IRAs and 401Ks or protecting children from creditors, divorce, and lawsuits. A "Probate Avoidance Plan" will not effectively deal with these issues. Instead, you should choose a "Family Protection Plan" form of estate planning that adequately deals with your whole family situation in order to protect your family.

MISTAKE #9. Focusing Only on Your Death.

The problem with most Estate Plans is that they contain only a Living Trust that deals with avoiding probate when you die. However, you are six times more likely to become *INCAPACITATED* than die in any given year. Often, the Lifetime Probate, called a Conservatorship, can be more cumbersome and expensive than a Death Probate. With this being the case, it is not prudent to have an Estate Plan that deals with only death. You need a plan that deals with controlling your assets both during your life and after your death.

MISTAKE #10. Not Having Current Health Care Documents.

Making Health Care decisions in the event of your incapacity is essential in order to maintain dignity and protect your family against being torn apart by not having guidance during difficult times. If you have your estate plan created before 2004, your Health Care Documents are outdated and need to be updated. The problem with most estate planning attorneys is that they do not have a formal maintenance program designed to constantly update your plan and make sure it complies with current law.

MISTAKE #11. Choosing the Wrong Type of “A-B” Trust, and Paying Unnecessary Capital Gains Taxes.

For married couples with estates in excess of \$1,000,000, it is often essential to have an “A-B” or “Bypass” Trust in order to save as much as \$900,000 in estate taxes at the death of the first spouse. However, there are 12 different types of “A-B” Trusts. Unfortunately, most Living Trusts choose one of the types of “A-B” Trusts that can result in unnecessary capital gains taxes at the death of the first spouse. Instead, you need an attorney who understands these different types of “A-B” Trusts, and can help you pick the one that’s right for you and your family.

MISTAKE #12. Not Protecting Your Children from Affluenza

If you leave too much money outright, there is a strong possibility that their life will be negatively affected. Lack of work ethic and lack of self esteem are common results of inheritances that are not received properly. In addition, your beneficiary may blow through their entire inheritance after incurring expenses they cannot afford on their own. This can lead to a collision course with bankruptcy. You need an attorney who understands these issues and can guide you in protecting your children from themselves when it comes to an inheritance.

MISTAKE #13. Not Protecting Your Children from Creditors

With the impending credit crisis in America, it is no surprise that bankruptcy filings have almost doubled in the last two years according to a report by the Center for American Progress. However, with the 2005 Bankruptcy Protection Act, many of these bankruptcy filers are declaring bankruptcy in an environment that is very favorable to their creditors. If any of your children suffer a bankruptcy, they may lose their inheritance as a result. Your Living Trust will likely not protect against this, so it is important to choose an attorney who can recommend a way to protect your children against bankruptcy.

MISTAKE #14. Not Protecting Your Children against Lawsuits.

It is estimated that if you divided the amount of damages awarded by juries by the number of Americans, you would find that each American citizen pays a “Lawsuit Tax” of between \$700 and \$800 per year according to the Federal News Service in 2004. Given the sheer number of lawsuits in American, it is vital to protect your children’s inheritance against losing their inheritance. However, unfortunately, most Living Trust do not do this. Your attorney must understand the complex legal methods necessary to protect an inheritance from creditors.

MISTAKE #15. Not Protecting Your Children Against Divorce.

In California, ½ of all marriages end in divorce. Therefore, it is possible that one or more of your children will divorce at some point in their lives. Unfortunately, if they have commingled their inheritance with their ex-spouse, they can lose ½ of their inheritance. It is a common misconception that an inheritance is protected from divorce. This is often not true, and you need an attorney who can protect your family from the unfortunate prospect of divorce.

MISTAKE #16. Not Protecting Government Benefits for Your Beneficiaries

One problem with inheritances is that they can disqualify your disabled beneficiaries from the right to receive government benefits, especially health care benefits. The loss of these benefits can rapidly decimate an inheritance, and can leave your beneficiary in a worst position than had they been disinherited. Instead, you must have a Special Needs Trust for beneficiaries who currently, or may in the future, receive government benefits. In addition, for beneficiaries who are not currently disabled, there must be a mechanism for allowing their trust to “morph” into a Special Needs Trust should they become disabled in the future.

MISTAKE #17. Not Having a Trust that Can Change to Comply With Future Laws.

One thing that’s for sure is that laws will change in the future. Because of this, you need to have an estate plan that can change as laws change, even after your death. I have encountered countless situations where it would be prudent to change a certain trust term in order to make it comply with current laws. However, the only way to accomplish this with most trusts is to engage in an expensive probate proceeding. Exactly what you were trying to avoid in the first place! Instead, you must have a trust that contains a way to change the trust terms in the future, without frustrating your original intent.

MISTAKE #18. Having a “Stale” Estate Plan.

A “Stale” Estate Plan is a plan that has not been updated within the past 3 years. Unfortunately, if you die with a stale plan, your Living Trust and other estate planning documents may not comply with current trust and tax laws. The results can be devastating to your family. As such, it is very important to make sure your attorney has a formal maintenance program in place to ensure that your plan will work not just now, but in the future as well.

MISTAKE #19. Not Considering Your IRAs and 401Ks.

The biggest tax most Americans will face at their death is the state and federal income taxes on their IRAs, 401Ks, and other qualified retirement plans. If there are also estate

taxes, this could result in a combined tax of over 70%! A Living Trust does not deal with these issues, and you should not leave your IRA or 401K to your Living Trust. Most attorneys have no experience dealing with these complex assets. As such, it is imperative that you hire an attorney who has experience in dealing with IRAs and 401Ks.

MISTAKE #20. Thinking that the Estate Tax is Going Away.

In 2001, President Bush signed into law a plan to eliminate estate taxes by 2010. Unfortunately, estate taxes were designed to return in 2011. Both current presidential candidates support an estate tax, and the current congress is in favor of estate taxes. As such, there is simply no chance that the estate tax is going away. As such, it is imperative that you start taking steps now to reduce your estate tax burden, since this type of planning is best done over the course of a number of years.

MISTAKE #21. Not Reducing or Eliminating Estate Taxes.

There is an old saying that “Nothing in life is for certain except for death and taxes”. When it comes to estate taxes, this is not really true. In most situations, they are optional, but only if you embark today on a strategy designed to reduce your estate tax liability. There are very few attorneys who have the experience, knowledge, and creativity necessary to avoid this unnecessary tax. Make sure you choose one who is up-to-date in this rapidly changing field.

MISTAKE #22. Giving Away All Your Assets to Reduce Estate Taxes.

Most Estate Planning attorneys deal with estate taxes by having a client give away significant assets to their kids. This may be fine for clients with a net worth above \$15million. Unfortunately, this can leave you with insufficient assets to meet your living expenses. Instead you must choose an attorney who can reduce estate taxes while at the same time allowing you access to those assets if you need them.

MISTAKE #23. Failure to Consider Generation Skipping Transfer Taxes.

You pay one set of estate taxes when you die and assets pass to your children. There is a second set of estate taxes when assets pass to your grandchildren, called the Generation Skipping Transfer Tax. If your Estate Plan fails to address this, your family may pay a great deal of unnecessary generation skipping transfer taxes.

MISTAKE #24. Failure to Address Your Grandchildren’s Health and Educational Needs.

Many clients leave everything to their children. While this is fine, and may be appropriate for you, I would like for you to consider the possibility of leaving a portion of your estate set aside for your grandchildren to pay for the health and educational expenses that they will incur as they get older. Considering that these are the two expenses that hold back our younger generations as they grow up, wouldn't it be nice to help your grandchildren as they face these challenges?

MISTAKE #25 Failure to Consider Asset Protection as Part of Your Estate Plan.

With the growth of lawsuits over the last few years, you'd be remiss not to protect your assets from your own creditors. Fortunately, if an estate plan is done right, you can reduce the risk of losing your hard earned wealth to creditors even as you reduce your estate tax burden. You need to select an estate planning attorney who understands how to incorporate asset protection into your estate plan.

Biography of Ward J. Wilsey



Ward Wilsey is an estate planning attorney based in San Diego, California. He is the developer of “Family Protection Planning™”; a unique form of estate planning that seeks to not only avoid probate, as is common with typical “Probate Avoidance Planning”, but to also protect his clients’ families against taxes, creditors, and the unintended consequences of inherited wealth.

Ward graduated from the University of California at San Diego with a degree in Economics. He obtained his law degree from the University of San Diego. After passing the California Bar, Ward obtained an advanced LLM in Taxation from the prestigious Washington University in St. Louis in order to further distinguish himself as an estate planning attorney.

Ward is a member of the American Bar Association, California State Bar Association, and San Diego County Bar Association. In addition, he belongs to the American Bar Association’s Section on Real Property, Probate, and Trusts.

Ward is a member of WealthCounsel, one of the preeminent estate planning groups in the country. He is also a member of InKnowVision, the Academy of Special Needs Planners, and the University of San Diego Planned Giving Committee.

Quickly establishing himself as an expert in estate planning, Ward is honored to be an instructor for the National Business Institute, which is one of the pre-eminent providers of Continuing Legal Education in the country. Ward has also been sought out by the California legal education provider Continuing Education of the Bar to be a contributor to treatises used by attorney’s throughout the State of California.

Ward has a great deal of experience helping clients with net worth’s in excess of \$1,000,000 plan their estates with Family Protection Planning. Ward seeks to erase the conventional paradigm that Probate-Avoidance is the main function of estate plan. Instead, Ward helps clients not only avoid Probate, but also protect their children from losing their assets to creditors, divorce, and lawsuits. At the same time, Ward instructs his clients to consider the effects that inherited wealth will have on their children.

Dedicated to the expanding his knowledge of estate planning, Ward attends over two weeks of continuing education each year, including events put on by WealthCounsel,

InKnowVision, the American Bar Association, the Southern California Tax Forum, and the Continuing Education of the Bar.

Ward enjoys golfing, playing guitar, running, and travel. He and his wife Katie have three sons, Jacob (3), Grayson (1), and Zachary (1). The Wilsey's live in Carmel Valley.