

## **An Introduction to Trusts and Estates**

Presentation for American Bar Association Community Outreach Committee

To Be Presented By:

Marc S. Bekerman  
Fleischman & Bekerman, LLP  
New York, New York

Thomas M. Featherston, Jr.  
Baylor University School of Law  
Waco, Texas

John J. Reddy, Jr.  
Bekerman & Reddy, LLP  
New York, New York

## **Pre-Death (Estate Planning)**

- I. Analyzing and Drafting for Non-Dispositive Issues
  - a. Health care issues – Use a health care proxy
    - i. Allows named agent to make decisions related to health care for the principal
    - ii. Take into account HIPPA rules regarding confidentiality of records
      - 1. Specifically refer to agent’s ability to review records in accordance with HIPPA
      - 2. Consider use of separate HIPPA release
    - iii. Execute several copies and circulate
      - 1. Client
      - 2. Agents named in instrument
      - 3. Primary care provider
      - 4. Specialists and other health care professionals
  - b. Quality of life issues – Use a living will
    - i. Allows client to make known their wishes as to whether they wish to be kept alive by extraordinary means
      - 1. “Pull the plug”
      - 2. DNR Orders
      - 3. Artificial or forced feeding
    - ii. Execute several copies and circulate
      - 1. Client
      - 2. Family

3. Doctors and health care professionals
  4. Clergy
- c. Property management and disability issues – Use a power of attorney
- i. Allows an agent to manage the property affairs of the principal
  - ii. Durable – Survives incapacity of the principal
  - iii. Springing – Effective at a future time
    1. Useful when a client does not want the agent to have authority immediately
    2. Generally is effective only upon the incapacity of principal
    3. Question as to when this occurs
      - a. Principal may not be able to certify due to incapacity
      - b. Doctors may be unwilling to certify
      - c. Principal may be unhappy that agent has sought certification and now seeks to act
    4. Potential ethical issue – Client says they have capacity; agent says that client is incapacitated
  - iv. All powers of attorney lapse when the principal dies

## II. Non-Tax Issues in Estate Planning

### a. Is client competent to make a Will?

i. Capacity to execute Will is lowest capacity in law (capacity to enter into a contract is higher)

### ii. Basic test is knowledge of:

1. “Nature and extent of assets” – Does client have a general idea as to what they own and approximate worth?

2. “Natural object of bounty”

### b. Obtain a family tree

i. List of close relatives (Natural object of testator’s bounty)

ii. Get addresses of relatives since these people may be necessary parties to probate proceeding after death

### iii. Note any special information

1. Distributees whose whereabouts are unknown

2. Beneficiaries who are “under a disability” or are “infants”

### c. Obtain a list of assets

i. Value of assets

### ii. Types of assets

#### 1. Liquid

a. Cash

b. Bank accounts (maybe not long term time deposits

(e.g., 5 year CD))

- c. Marketable securities (e.g., stocks, bonds, mutual funds)

## 2. Illiquid

- a. Tangible personal property
  - i. Cars
  - ii. Boats
  - iii. Jewelry
  - iv. Artwork
  - v. Household furnishings
  - vi. Clothing and personal effects
- b. Real estate
  - i. Residences
  - ii. Vacant land
  - iii. Land with improvements
- c. Business interests
- d. Mortgages and promissory notes
- e. Royalties and copyrights
- f. Rights
- g. Reversionary or remainder interests
- h. Interests in trusts
- i. Powers of appointment
- j. Annuities

3. Remember to review:

a. Life insurance

- i. Often not an asset during lifetime, but needs to be considered in creating estate plan
- ii. Life insurance on client's life owned by another (individual or trust)
- iii. Life insurance owned by client on someone else's life

b. Retirement benefits

- i. May have limited access now, but will be an asset of an estate and could require special planning
- ii. 401(k) accounts
- iii. IRA accounts
- iv. Pensions

iii. Manner held

- 1. Client's name alone
- 2. Joint (with or without right of survivorship)
- 3. Designated beneficiary
- 4. In an entity (e.g., a revocable trust)
- 5. Consider obligations of client that limit ability to dispose of property

- a. Agreements
  - i. Marital agreements
  - ii. Business agreements (e.g., buy-sell agreements with partners)
- b. Family rights
  - i. Right of election
  - ii. Exempt property
- d. Ask client how and when they wish to dispose of property
  - i. Who are the intended beneficiaries? These may not be the “natural object of the testator’s bounty”.
  - ii. Should the beneficiaries receive their interests outright or in trust?
  - iii. Providing for the surviving spouse
    - 1. Right of election
    - 2. Agreements between spouses
  - iv. Providing for minors
    - 1. Nomination of a guardian
    - 2. Disposition of property to minor
      - a. Outright
      - b. Trust
        - i. Testamentary trust
        - ii. UGMA/UTMA account
  - v. Rights of family under state law – Exempt property which is not subject to creditor’s claims

vi. Jointly held property

1. Surviving tenant obtains full title to jointly held assets upon death of co-tenant (“passes by operation of law”)
2. Not part of estate disposed of under Will
3. Determine whether bank accounts are joint with right of survivorship or convenience account
  - a. Review passbook and signature card to confirm intent is properly reflected in the bank’s paperwork
  - b. If not labeled a convenience account, could lead to later litigation to determine whether the client intended the surviving joint tenant to have the remaining balance of the account

vii. Property with designated beneficiary

1. Will pass to beneficiary if the beneficiary survives
2. Examples include retirement plans and life insurance

viii. Lifetime gifts (non-tax issues)

1. Can the client afford to make lifetime gifts?
2. Does the client wish to make lifetime gifts?

e. Implementation of estate plan

i. Drafting issues

1. Cautions and considerations
  - a. Be careful when using boilerplate language from either a drafting program or a formbook

- b. If doing revocable trust, be sure to expressly provide for the Grantor's retained powers
2. General format of dispositive instrument
- a. Direction of payment of debts, expenses, including apportionment of taxes (if overriding default statute, be careful not to establish an infinite loop, especially on tax apportionment)
  - b. Devises of real property
    - i. Be careful if devising to more than one beneficiary since multiple tenants in common can cause a problem
    - ii. Consider whether sale should be directed
      - 1. May save need for a partition proceeding later
      - 2. May allow estate to use expenses of sale as a deduction
      - 3. May allow estate to use carrying charges as a deduction
    - iii. If there is a mortgage on the property
      - 1. Should mortgage be satisfied before property is transferred?
      - 2. Should property be transferred subject to mortgage?

3. If transferred subject to mortgage:
  - a. Should there be an additional bequest to beneficiary?
  - b. Should there be offsetting bequests to other beneficiaries?
- c. Specific bequests of tangible personal property
  - i. Consider whether costs of distribution (moving expenses, storage, insurance) should be borne by the beneficiary or the estate
  - ii. Division among a class of beneficiaries
    1. What if beneficiaries cannot agree?
    2. If using executor as ultimate decision maker, what if executor is member of class?
  - iii. Future valuation issues
    1. Example – Two items of personal property have similar values currently, but dramatically different values at time of death. Should a general legacy be given to beneficiary with less valuable asset

to equalize the two “equal  
beneficiaries”?

- d. General legacies
- e. Residuary clause
- f. Nomination of fiduciaries
  - i. Executors
  - ii. Trustees if trusts are created under Will
  - iii. Guardian of minor children if appropriate
- g. Powers granted to fiduciaries
  - i. State law provides for default powers
  - ii. Additional powers
  - iii. Consider enumerating desired powers in case of a change of law, or a change in residence (i.e., “In addition to all powers granted by the law of the District of Columbia, the following powers are hereby granted:”)
  - iv. Examples of powers to consider:
    - 1. Hire employees
      - a. Attorneys
      - b. Accountants
      - c. Agents
    - 2. Distributions

a. Should distributions in kind  
be allowed?

b. Should non pro-rata  
distributions be allowed?

3. Power to borrow against assets (if  
corporate fiduciary, consider whether  
they should be allowed to borrow  
from self)

h. Miscellaneous

i. Possibility of lapsing bequest (treatment of a  
bequest to a beneficiary who predeceases the  
decedent)

ii. Survivorship clauses, including  
simultaneous death clause and equalization  
clause

iii. In Terrorem clauses

iv. Exercises of powers of appointment

v. Use of formula and fractional bequests

i. Attestation clause

III. Wills - Execution issues

a. Should be supervised by an attorney

i. Sample script: Have you read this instrument? Do you understand  
the contents of this instrument? Do you declare this instrument to

be your last will and testament? Would you like these persons to be the witnesses to your will?

- b. Must usually have at least two disinterested witnesses
  - i. Have witnesses meet and speak with testator for a period of time so they can later testify, either by affidavit or deposition, that they believe the testator was competent to make a Will
  - ii. Witnesses may wish to make diary entries or memos to file to reflect that they met the testator, that they believed the testator to be competent to make a Will, that they witnessed the execution of the Will, and that the execution was in accordance with state law
- c. Execute only one original which should then be kept in a safe place
  - i. Given to client
  - ii. Retained by attorney
- d. Consider use of self-proving affidavits if allowable under local law
  - i. No need to produce witness unless a party to the probate proceeding requires production
  - ii. In a contested probate, the affidavits will not relieve the proponent from their duty to produce the attesting witnesses for examination by the objectant

#### IV. Trusts

- a. Intervivos trusts are either irrevocable or revocable

- b. Testamentary trusts are created under a decedent's Will (Like all other aspects of a decedent's Will, a testamentary trust has no meaning until after the testator has died and their Will is admitted to probate)
- c. Why have a bequest placed in trust?
  - i. Estate planning considerations (e.g., tax)
  - ii. Spendthrift beneficiaries
  - iii. "Creditors and predators" – Can include current spouse who may one day become an ex-spouse
- d. How long should trust go for?
  - i. Look to reason for trust
  - ii. Possible lengths
    - 1. Life of income beneficiary
    - 2. Life of another person
    - 3. Until current beneficiary reaches a certain age
    - 4. Specific number of years
- e. Drafting issues
  - i. Trustees
    - 1. Who are the trustees?
      - a. Family member
      - b. Friend or trusted advisor
      - c. Corporate fiduciary
      - d. Grantor or related person as defined in IRC
      - e. Non-adverse party as defined in IRC

2. Compensation (i.e., commissions)
    - a. State law
    - b. Fee schedule
    - c. Provide for no compensation
  3. How should successor trustees be selected and appointed?
    - a. By instrument
    - b. By fiduciaries
  4. What powers should the trustees have?
    - a. Consider all powers granted by state law
    - b. Consider enumerating certain powers in case of change of state law or trust situs
    - c. Powers to shift interests of beneficiaries
      - i. Accumulate income
      - ii. Invade principal – Discretionary or ascertainable standard
      - iii. Make adjustments between principal and income
- ii. Investment issues
    1. Delegation to professional
    2. Restrictions or lack thereof
    3. Duty to diversify
    4. Ability to invest in stocks, bonds, mutual funds (including common trust funds of a corporate fiduciary)

iii. Beneficiaries

1. Who are the beneficiaries?
2. When should beneficiaries be entitled to proceeds of the trust?
  - a. Determine purpose of trust
  - b. If due to age, consider paying out in stages versus payout of entire trust at a chosen age
3. Should the beneficiaries have any special powers?
  - a. Power to withdraw from trust
  - b. Power to invade for own benefit based upon an ascertainable standard
  - c. Power to remove and/or appoint trustees
4. Nature of interests
  - a. Traditional principal/income trust
  - b. Annuity trust and unitrust
  - c. Trust where trustee has discretion to distribute or accumulate income

f. Liquidity issues

- i. Consider that a surviving spouse living on an income interest from a marital trust may have a difficult time maintaining their previous standing of living
- ii. Possible solutions:

1. Give trustee power to invade either pursuant to a standard or purely discretionary
  2. Give spouse power to withdraw limited to either a 5&5 power or an ascertainable standard
- g. Interests sometimes retained by grantor
- i. Property interest
    1. Income
    2. Annuity or unitrust
    3. Reversion
  - ii. Fiduciary interests - Act as trustee or co-trustee
    1. Powers
      - a. Power to revoke all or part of trust
      - b. Power to shift income (sometimes called a “spray” power)
      - c. Power of appointment over remainder
      - d. Power to remove trustee
      - e. Power to appoint trustee
      - f. Power to shift interests among beneficiaries
      - g. Power to change identity of beneficiaries
      - h. Power to deal with trust (e.g., power to substitute property of equal value)

2. Need to examine retained powers and interests closely to ensure that the retention does not undermine the purpose of the trust

h. Revocable trusts

- i. Grantor usually serves as trustee and can manage property
- ii. Grantor usually entitled to all income generated
- iii. Grantor can usually invade principal for own benefit
- iv. Grantor can revoke and reclaim trust assets
- v. Trust becomes irrevocable upon death of grantor (administered by co-trustee or successor trustee upon death or disability of grantor)
- vi. Revocable trusts have no tax consequences
  1. No income tax consequences under grantor trust rules
  2. No gift tax consequences since no gift tax payable on making of a revocable gift (see Treas. Reg. §25.2511-2(b))
  3. No estate tax consequences since a revocable gift will be included in the estate of the grantor (see IRC §2038)
- vii. Use of revocable trusts as will substitutes
  1. Use as part of a testamentary plan that includes a Will that pours over any probate assets into the revocable trust since there is almost always some items in decedent's name and not transferred to trust
    - a. Examples of assets that are usually not transferred prior to death

- i. Salary checks, social security checks
  - ii. Personal property
  - iii. Cash on hand (including traveler's checks)
2. Pour-over Will directs executor to distribute assets to revocable trust
  - a. Generally needs to be offered for probate in same manner as a traditional Will (may qualify for small estate proceeding)
3. May be easier to contest an inter-vivos transfer than a testamentary disposition of property if the capacity requirements are different
4. Can avoid probate if property is transferred into trust (must register all property in name of trust), which may be desirable:
  - a. Publicity
  - b. Delay
  - c. Filing fees
  - d. Ancillary probate
  - e. May be very helpful if names or locations of distributes are unknown
5. Grantor no longer owns property during life of trust under state law (although may be deemed owner for income tax purposes under grantor tax rules)

- i. Beneficiaries
  - i. Income beneficiaries (usually current beneficiary)
    - 1. “Simple” trusts require annual distributions of all income
    - 2. “Complex” trusts allow trustee to add undistributed income to principal
  - ii. Remainder beneficiaries (usually future beneficiary)
  - iii. Other types of non-remainder interests (e.g., a current beneficiary of an annuity trust or a unitrust that are usually associated with charitable split-interest trusts or estate freeze situations as provided for in IRC §§2701-2704)
- j. Where there are multiple beneficiaries, consider using one fund for all beneficiaries (“pot trust”) versus dividing trust into separate shares for each beneficiary

V. Comparison of Wills and Revocable Trusts

<u>Wills</u>	<u>Revocable Trust</u>
Effective upon probate, which usually can occur only after death	Usually effective immediately, although funding of trust may occur at a later time
Probate is a judicial proceeding which may require notices and service of process	Grantor usually retains right to revoke trust, in whole or in part
Low level of capacity needed for execution	Since trust is an agreement between grantor and trustee, grantor must have capacity to entire into a contract, which is usually higher than capacity to execute a Will
Does not assist in disability planning – Need a separate instrument, such as a power of attorney, to manage property, and a health care proxy to allow agent to attend to principal's personal needs	Provides for incapacity of grantor by allowing co-trustee or successor trustee to continue to manage assets in trust regardless of grantor's capacity; Should consider a health care proxy to attend to grantor's personal needs
Can provide for guardians of minor children	Generally does not provide for guardians of minor children
Operates only on "probate" assets, or "testamentary" assets (assets either in client's name alone, or where beneficiary predeceases client)	Operates only on those assets actually transferred to trust. For plan to be effective, most assets are usually placed in trust during lifetime and a "pour-over" Will is used to transfer remaining assets at death

VI. The Federal Transfer Tax System— An Overview

a. Federal Transfer Taxes

- i. The Estate Tax
- ii. The Gift Tax
- iii. The Generation-Skipping Tax

b. Old vs. New

- i. The bifurcated system - pre-1977
- ii. The unified system - 1977-2001
- iii. Reformation - post-2001

c. The Basic Formula:

Gross Estate

- Deductions

Taxable Estate

+Post '76 Taxable Gifts

Tax Base

Gross Gift

- Deductions

- Exclusions

Taxable Gift

+Prior post '76 Taxable Gifts

Tax Base

d. State Death Taxes

- i. Estate Taxes
- ii. Inheritance Taxes
- iii. "Credit" Tax
- iv. Limited to a Deduction (2005)
- e. IRS's Internet Website: [www.irs.gov](http://www.irs.gov)

VII Introduction To Transfer Tax Principles After Estate Tax Reform (2002)

- a. The Basic Formula:

$$\begin{array}{r}
 \text{Gross Estate} \\
 - \text{Deductions} \\
 \hline
 \text{Taxable Estate} \\
 + \text{Post '76 taxable gifts} \\
 \hline
 \text{Tentative Tax Base}
 \end{array}$$

- b. Gross estate
  - i. Probate
    - a. real property
    - b. stocks & bonds
    - c. mtgs., notes & cash
    - d. misc. property
  - ii. Non-Probate
    - a. insurance
    - b. JTWRORS
    - c. multiple party accounts
    - d. annuities

- iii. General Powers of Appointment
- iv. Special Lifetime Transfers
  - a. 3 yr. Rule
  - b. retained life estate
  - c. effective at death
  - d. revocable
- v. Q-Tip Property
- c. Deductions
  - i. Ordinary
    - a. funeral
    - b. administration expenses
    - c. debts & mtgs.
  - ii. Special
    - a. marital deduction
    - b. charitable deduction
- d. Inter vivos gift in excess of “annual exclusion” amount and which is not included in the gross estate as a special lifetime transfer.
- e. Tentative Tax Base: The amount on which the tentative tax is computed; the net tax owing is the tentative tax reduced by certain credits (eg. the unified credit—\$345,800 until 2004).

Applicable Exclusion Amount:

2002, 2003	\$1,000,000
2004,2005	\$1,500,000
2006-2008	\$2,000,000
2009	\$3,500,000

Maximum Rate:

2002	50%
2003	49%
2004	48%
2005	47%

2010	---
2011	\$1,000,000

2006	46%
2007-2009	45%
2010	---
2011	55% (plus 5% surcharge)

VIII. Estate Planning with tax issues

i. Federal gift tax (IRC §2501)

1. Similar concept to estate tax in that it is an excise tax on the transfer of wealth
  - a. Applies to gifts during lifetime
  - b. \$1,000,000 lifetime exemption amount - Remember that estate tax exemption is scheduled to be larger than the gift tax exemption
2. Taxable gifts must be reported annually on a Federal Gift Tax return (Form 709)
3. Unless otherwise specified, the gift tax liability must be satisfied by the donor
4. Lifetime exemption amount must be used completely before donor pays any gift tax - Any exemption amount used will reduce the exemption amount available to the decedent's estate to reduce the estate tax liability
5. Can have a completed gift for property purposes, but an incomplete gift for tax purposes
6. Annual exemption of \$12,000 per year per donee for gifts of present interests (IRC §2503(b))
  - a. Married couples can exempt \$24,000 per year per donee by election to split gifts (IRC §2513)

- b. This amount will increase in \$1,000 increments as it is indexed for inflation (See Tax Reform Act of 1997)
      - c. Must be a gift of a present interest
- 7. Can also exclude tuition and medical expenses if paid directly to service provider (IRC §2503(e))
- 8. Tax advantages of gifts
  - a. Gift tax is considered tax-exclusive since the tax is paid out of non-transferred funds
    - i. Added back to estate for tax purposes if donor dies within three years of gift tax payment
    - ii. Estate tax is considered tax-inclusive since the dollars that pay the estate taxes are themselves taxed
  - b. Future growth and income is transferred to beneficiary without any further tax consequences to donor (sometimes referred to as a “freeze” since value of transferred property is frozen for transfer tax purposes)
- ii. Federal estate tax (Internal Revenue Code “IRC” §2001 et seq)
  - 1. Excise tax on transfer of wealth reported on Form 706

2. Applicable exemption amount (formerly known as “unified credit”) currently equals \$2,000,000, gradually increases to \$3,500,000 for decedent’s dying in 2009, subsequently repealed in 2010 and reinstated at a \$1,000,000 level in 2011 (See Economic Growth an Tax Relief Reconciliation Act of 2001 “EGTRRA”)
3. Generally imposed on all assets that decedent has some form of control over whether passing by will or by operation of law (IRC §2031)
  - a. Can be testamentary or non-testamentary asset
  - b. If non-testamentary asset, decedent usually had some form of control
    - i. Power to revoke
    - ii. Power of appointment
    - iii. Trust created by decedent where they retained an income interest and died during the term of the trust
4. Deductions generally allowed for administration expenses, claims against the estate, amounts passing to the surviving spouse or to a qualified charity, and now for state death taxes paid (See IRC §§2053-2056)
5. Marital deduction

- a. An unlimited marital deduction is available where spouse is a citizen and the interest “qualifies” (See IRC §2056)
- b. Tax deferral, not tax forgiveness, since will be taxed in estate of surviving spouse
- c. All non-terminable interests qualify
- d. Certain terminable interests may qualify
  - i. Most common qualifying terminable interest is a trust where an election is made on the federal estate tax return to qualify the surviving spouse’s interest in the trust for the marital deduction (commonly known as a QTIP trust).
    1. QTIPs are popular since the testator can control the disposition of the funds after the death of the surviving spouse
    2. Income must be paid at least annually to the surviving spouse for the remainder of their life
    3. Principal can only be invaded for the benefit of the surviving spouse

- 4. As part of the election, it is agreed that the trust will be included for estate tax purposes in the estate of the surviving spouse
    - ii. Another trust still used occasionally to obtain the marital deduction is where the surviving spouse is given a general power of appointment of the trust principal
  - e. Must limit survivorship clause on spouse's interest to no more than 6 months
  - f. Consider using equalization clause in instrument, or equalizing estates during lifetime, to minimize overall estate tax
- 6. "Credit shelter trusts" allow for full utilization of unified credit
  - a. There may be a tax benefit in refraining from leaving all property to the surviving spouse and using the marital deduction to eliminate the estate tax liability
    - i. Example – Two spouses together own \$3,500,000 in property. If the estate of the first spouse is transferred in its entirety to the surviving spouse, there will likely be

federal estate tax due upon the death of the second spouse. However, through use of the unified credit, it may be possible to pay no federal estate tax in either estate.

- b. Credit shelter amount is often placed in a trust that is drafted with certain goals
  - i. The trust will not be included in the estate of the surviving spouse for estate tax purposes
  - ii. Surviving spouse can still have access to money as needed
    - 1. Independent trustee has discretion to pay income or principal
    - 2. Power to withdraw \$5,000 or 5% of trust on an annual basis (power may be exercisable only for a day)
- c. Problems of utilizing unified credit
  - i. Each spouse must have enough property in their own name to utilize their unified credit
  - ii. All jointly owned property goes to surviving co-tenant; so if all property is held by spouses jointly, surviving spouse will take all property by operation of law

- iii. Note that although these issues may be addressed post-mortem through disclaimers, but it can be difficult to achieve and potentially risky
  - iv. May have state death tax consequences if state exemption is less than federal exemption
- d. With exemption amount increasing, consider following:
- i. Will second estate likely be subject to estate tax?
  - ii. Potential impact on estate plan by spouse exercising right of election
  - iii. If full exemption is used, are there sufficient funds to take care of surviving spouse
  - iv. Potential state death taxes on first to die if using maximum federal exemption
- e. Funding with a pecuniary versus a residuary bequest
- i. Pecuniary bequest guarantees desired amount into credit shelter trust
    - 1. No growth
    - 2. No income

ii. Residuary bequest

1. May give more or less to credit shelter depending on performance of portfolio during estate administration
2. Will also give trust an interest in income earned by the estate during administration

7. Taxable estate is computed by subtracting deductions from the gross estate
8. Tentative tax is computed by applying rates to taxable estate
9. Estate tax due is then computed by applying available credits, primarily applicable exemption amount, to tentative tax
  - a. Note discussion of state estate taxes below with regard to decoupling
  - b. Note there is no longer a credit for state death taxes

iii. State estate tax

1. Prior to enactment of EGTRRA, most states had a tax equal to the amount of state death tax credit available from federal tax law
  - a. Resulted in no increase in estate tax to estate



## **Post-Death (Estate Administration)**

- I. Pre-Appointment
  - a. Client Interview
    - i. Gather information
    - ii. Review terms of Will if one exists
    - iii. Get original Will
      1. If original cannot be located and decedent is known to have had a safe deposit box, arrange to search box
    - iv. If no Will, who is entitled to administer the estate under law
      1. Distributees usually have first opportunity
      2. If no distributees known, or willing to serve, local law usually provides an administrator of last resort
    - v. Determine persons interested in the appropriate proceeding to appoint a fiduciary
      1. Probate proceeding
        - a. Distributees
        - b. Persons who receive more in prior Wills (usually must have original Will filed with Court)
        - c. Statutory requirements
          - i. Attorney General if charities
          - ii. Administrator of last resort if no known kin
        - d. Other persons who may be entitled to notice
          - i. Legatees

- ii. Alternate fiduciaries
  - 2. Administration proceeding (if there is no Will)
    - a. Persons with an equal or greater right to administer the estate than the petition must usually receive citation
    - b. Persons who have an inferior right to act as a fiduciary are generally entitled only to notice
    - c. Again consider statutory requirements
  - 3. Consider use of statutory small estate provisions
- II. Process to Appoint a Fiduciary
  - a. Prepare appropriate documents
    - i. Original Will
    - ii. Petition
    - iii. Citation or Waiver of Citation
    - iv. Notices
    - v. Supporting papers
      - 1. Affidavit of attesting witnesses
      - 2. Affidavit of kinship
      - 3. Affidavit proving a correct copy
      - 4. Affidavit of due diligence
  - b. File papers with Court
  - c. Attend Court on return of citation if appropriate
  - d. Appointment of Fiduciary

- i. May be required to post a bond
- ii. Obtain letters from Court to evidence appointment

### III. Post-Probate

#### a. Identifying and marshalling assets

##### i. Locating assets

1. Request post office to deliver decedent's mail to fiduciary or attorney for fiduciary
2. Contact decedent's employer (or most recent employer)
3. Contact decedent's union or other business organization if applicable
4. Review decedent's income tax returns concerning passive income items reflecting an investment
5. Contact appropriate state officials concerning abandoned property (including state officials for other states where decedent is known to have lived or maintained assets)
6. Open safe deposit box if not already done

##### ii. Types of assets

1. Bank accounts and cash
2. Stock & securities owned by the decedent
  - a. Certificate held by decedent
  - b. Account at brokerage firm
3. Benefits payable to the estate
  - a. Life insurance

- b. Death benefits
  - 4. Retirement accounts
    - a. Accounts maintained by decedent
    - b. Accounts maintained by employer
  - 5. Wages owed to the decedent
  - 6. Real estate
  - 7. Tangible personal property
  - 8. Business interests
  - 9. Interests in trusts
- iii. Need to distinguish between testamentary assets and non-testamentary assets
  - 1. Testamentary assets
    - a. Pass through estate
    - b. Rightfully collected by fiduciary
    - c. Assets in:
      - i. Decedent's name alone
      - ii. Held in joint name or with a designated beneficiary where other party predeceased the decedent
  - 2. Non-testamentary assets
    - a. Do not pass through estate
    - b. Payable directly to named beneficiary
    - c. Assets held:

- i. Joint with right of survivorship (but be careful of “Convenience Accounts”)
      - ii. In Trust For accounts
      - iii. Payable on Death accounts
    - d. May be reached for payment of estate taxes if appropriate
    - e. May be reached for funeral expenses or other administration expenses if estate is insolvent
  - iv. Marshaling assets
    - 1. General requirements
      - a. Death certificate
      - b. Proof of appointment
    - 2. Specific requirements
      - a. Releases of lien
        - i. Real property
        - ii. Personal property
      - b. Passbooks or lost passbook affidavits
      - c. Stock powers
      - d. Affidavits of domicile
- b. Ascertaining, deciding and paying claims
  - i. Fiduciary may have obligation to ascertain the decedent’s creditors and determine whether they wish to file a claim against the estate

- ii. Fiduciary can impose certain requirements regarding the filing of a valid proof of claim against the estate
- iii. A fiduciary should exercise caution in making distributions to estate beneficiaries until the creditor's period has ended
- iv. Fiduciary has the right to determine the validity of a claim and pay only those claims they believe to be valid (keep in mind that a rejected creditor will have recourse to the Courts for payment of a debt that they believe to be properly owed by the estate)

c. Estate taxes

i. Federal estate taxes

- 1. Threshold for filing of federal estate tax return (Form 706) will depend on year of death – Equal to estate tax exemption amount

- a. Both testamentary assets and non-testamentary assets are includible in determining the gross estate – Certain property not in the decedent's possession at the time of his death may be brought back into the estate for the calculation of the gross estate for estate tax purposes
- b. Valuation is generally on the date of death, although an alternate valuation date is available if it will lower the estate tax due (IRC §2032)



- a. Informal if permitted under local law
  - i. Can be in any form
  - ii. Be sure to provide sufficient information for beneficiaries to understand what has occurred during estate administration
  - iii. Usually completed by a receipt and release
  - iv. Issues
    - 1. Fiduciary accounting to self (i.e. as executor to self as trustee)
    - 2. Beneficiaries who cannot sign off
      - a. Minors
      - b. Persons under disability
- b. Judicial
  - i. Court specified format
  - ii. Process to “interested persons”
  - iii. Court must approve whether or not objections are filed
  - iv. If objections are filed, must be resolved prior to completion
  - v. Usually completed by a Decree on Accounting

#### IV. Post-Mortem Planning

- a. Renunciations (also known as disclaimers)

- i. Federal requirements – IRC §2518
- ii. State law requirements
- iii. If done correctly, treats person renouncing as if they predeceased the decedent
- iv. See terms of Will and anti-lapse statute if applicable to determine consequences
- v. Popular method of funding the credit shelter trust since it provides maximum flexibility as to the amount funding the trust and the assets used to do so
  - 1. Note there are potential pitfalls
    - a. Spouses who do not disclaim
    - b. Spouses who cannot disclaim (i.e., under a disability)
    - c. Spouses who use the property, thereby invalidating a potential disclaimer
  - b. Electing a fiscal year
  - c. Annual distributions of income

## Common Problems of Planning and Administration

- I. Typical ethical traps and dilemmas
  - a. Representing both spouses
    - i. In estate planning
      - 1. Insufficient bequest to surviving spouse
      - 2. QTIP trusts
      - 3. Health care proxies and powers of attorney where agent is not the other spouse
    - ii. In estate proceeding of first-to-die
      - 1. Representing an objecting surviving spouse in a contested probate
      - 2. Representing the estate where the surviving spouse is objecting to probate
  - b. Attorney-client privilege - The person who pays the bill may not be the client
  - c. Attorney-draftsman as executor
  - d. Informing the client concerning powers of attorney, health care proxies, etc. – Unpaid Time vs. Duty to Inform (To inform a client sufficient concerning these documents will take time that may go uncompensated)
- II. Marital deduction planning – Certain interests cannot qualify for QTIP treatment
- III. Liquidity
  - a. Use of life insurance to pay estate taxes

- b. Life insurance in estate vs. life insurance trusts
- IV. Destruction of previous Wills
- V. Videotaping of Will execution
  - a. Will the videotape help the probate process?
    - i. Appearance of testator in videotape
      - 1. Need low level of capacity to execute Will
      - 2. Impact of seeing a testator with diminished or questionable capacity
    - ii. If execution is videotaped, must videotape be disclosed if objections are filed, but not specifically requested by objectant
- VI. Simultaneous death clauses
  - a. Do not create infinite loop (e.g., husband and wife each have Wills with a clause deeming that the other survived)
  - b. Effect on tax planning – May need to have spouse with less assets in own name be deemed to survive other spouse in case of simultaneous death
  - c. Limit survivorship of spouse to six months – Otherwise can lose marital deduction
  - d. Definition of simultaneous death – “Common accident or disaster” – Can present its own problems
- VII. Tax apportionment clauses
  - a. Examine default provision under state law
  - b. Treatment of non-testamentary assets
  - c. Payment of tax due

i. By residue

1. Impact on residuary beneficiary

2. Impact on availability of tax deductions and interrelated  
computations

ii. By each beneficiary proportionately

VIII. Convenience accounts

## **Income Taxation Of Trusts And Estates In A Nutshell**

- a. Income taxation of trusts and estates is provided for by Subchapter J of the IRC (§§641-691)
  - i. IRC §641 requires a trust to pay tax on its income
  - ii. Rate structure for trusts is much narrower than individual rates
  - iii. Income tax rules for trusts and estates are essentially identical except for a different exemption amount
    - 1. Estates - \$600
    - 2. Simple trusts - \$300
    - 3. Complex trusts - \$100
  - iv. Generally, a trust will pay tax on its income to the extent that the income is not distributed to the beneficiaries (i.e., accumulates income)
  - v. Trusts are entitled to deductions, credits and exemptions as allowed for by Subchapter J
- b. Grantor trust rules
  - i. Trusts were used to shift income to beneficiaries in lower income tax brackets
  - ii. Response was IRC §§671-678 which provides that the Grantor will be treated as owner of trust for income tax purposes if certain circumstances are present
  - iii. Indicia of grantor trusts
    - 1. Revocable trusts are always grantor trusts

2. Trusts where grantor has a large enough reversionary interest in trust property
  3. Grantor has power to control beneficial enjoyment (but see IRC §674 for allowable powers that will not trigger grantor trust rules)
  4. Power to deal for less than full and adequate consideration
  5. Power to borrow without adequate interest or security
  6. Borrowing of trust funds
  7. Power to exchange trust property for property of equal value
  8. Certain “General Powers of Administration”
- iv. Powers and interest of non-grantor spouse are attributed to grantor spouse
  - v. Grantor can be deemed owner of part of trust under grantor trust rules where the activating item applies only to a portion of the trust
  - vi. Grantor trust rules have turned into a very powerful estate planning tool since the grantor will be liable for the income tax generated by the income of the trust regardless of the disposition of the income. The payment of this income tax liability is not a gift since it is a legal obligation of the grantor. See Revenue Ruling 2004-64.