Legacy Planning for Estates and Businesses

Basics for a Solid Foundation for Your Estate Plan

by Attorney David E. Walker

Central Controlling Mechanism

Most of you are probably aware after hearing the old adage for many years, "you must have your will done." For that reason most of you, when you finally get around to it, go out find an attorney and have that attorney prepare a will for you. You may also be aware that without a will the state will determine how things are distributed at your death. Therefore, most of us have been conditioned to think the will is the cornerstone or foundation of an effective estate plan. However, that's not necessarily true. Just having a simple will could be putting your loved ones through a long and arduous task called, "Probate."

Probate is the legal process of transferring assets from the deceased person to those people whom the deceased person would like to have their assets. Sounds simple, however, it could be the start of a long and expensive process that could totally be avoided. Therefore, the foundation of your estate plan should include a revocable trust. Having a revocable trust sets up a central controlling mechanism that will avoid probate, spell out in detail how things are to go to those you would like to

have your assets after your death. I will get into more details about trusts later but for now let's go over some very important ancillary items that will work in concert with the trust to build the best foundation for your estate plan.

Powers of Attorney

One of the most important items you can establish before you actually need it is a health care power of attorney. The power of attorney for health care does several things that are very important as a foundational piece of a solid estate plan. First, the health care power of attorney allows you, the principal, to appoint an agent to make important health care decisions if you become incapacitated and can't make decisions for yourself. You avoid a long, expensive and arduous task for your loved ones that would otherwise have to hire attorneys, petition for guardianship over your affairs before they can act on your behalf. By setting up these powers of attorney before hand you avoid hiring attorneys, petitioning the courts, and having to deal with delays and hassles.

HIPAA – What you need to know about Health Care Powers of Attorney

These days, people are more informed about the issues of health care. We are inundated by the latest developments in health care as it deals with our government and private health care providers as well. Some of you may even be familiar with the new federal mandate called HIPAA, which is an acronym for Health Insurance Portability and Accountability Act. Your primary doctor seems to always ask you to sign off on HIPAA during your routine doctor visits. They may say something like, "we just need to update your medical records." Sounds simple right, however, that simple acronym has health care providers running scared.

The HIPAA rules says no one can speak to anyone about the care of any individual unless that individual (the patient) has a signed HIPAA release saying it's okay to share information with your loved one. If the health care provider does not have this signed release ahead of time the health care provider can't legally share or talk about your care with your loved one without fear of being sued for their breach of HIPAA rules. Therefore, a key foundational piece is to have your health care power of attorney updated to name agents, including a couple of backup agents, in case the primary agent is unable to act.

Also, even if you have already prepared a medical power of attorney, make sure that it includes that all important HIPAA release so that doctors will be allowed to share your private information with your agents.

Durable Power of Attorney

By the same token there is another power of attorney that needs to be mentioned here. It's known as the "Durable Power of Attorney." It has the same idea as the health care power of attorney with the exceptions that: 1) It does not require incapacity for your agents to act; and 2) It does not deal with health care decisions per se. It could however, be used to move a loved one to a different facility if your agent thinks you could get better care at a different facility. As a foundational piece to your solid estate plan it plays the role of allowing your loved one to act on your behalf for business matters, such as: banking, dealing with brokers (real estate, stocks, etc.) filing taxes, handling a family business, etc.

Even if you already have these documents in place they may or may not be up to date. Some key provisions such as the ones mentioned above could be missing from your documents. For the Durable Power of Attorney look to see if your document has provision that will allow you to do estate planning for your loved one should they need to organize their affairs in such a way to help you qualify for State of Federal aid. Your document should allow you to enter your loved ones retirement accounts in case you need to pay for his or her care and other resources are running low or you have already exhausted them.

Another key idea that you will want to keep in mind when preparing both health care and financial powers of attorney is to name multiple backup agents. Normally a husband and wife will name each other as their primary agents. However, even naming a son or daughter as a secondary agent may not be enough. There may be an occasion where you will need a third agent in place. For example, if both parents are in a common accident, such as a car accident, this may happen at a time where the secondary agent is unavailable. Therefore, it is a common practice to have a third person who will be available to assist you in your time of need. By having a third person named as a successor agent gives you more flexibility and adds an additional resource should you need the agent to spring into action. This is extremely important if your primary and/or secondary agents travel out side your geographical location and may not be available at a time when you need them.

Your Right to Die – Advance Directives or Living Wills

We have had some very important news events involving families in crisis because of differing opinions on a loved ones rights to die. Usually these crises are surrounded by the fact that the loved one in question is on life support or being kept alive by artificial means, i.e. ventilator or respirator or in some cases a feeding tube. If it is your wish not to be kept alive this way you have a right to be heard. However, if you are this far along and can't voice your desires it is best to have prepared a document before hand spelling out your wishes. This document goes by several different names depending upon which state you live in. Some states, such as New Hampshire calls the document a "Declaration." Other states call the document, "Advanced Directive," "Medical Directive," or "Living Wills" and so on.

These advance directives are simply a way to show a doctor or caregiver that you do not want to be sustained by machines. These documents are very important when a hospital has a policy not to take termination orders from a health care power of attorney agent. For example, you have given your eldest child power of attorney over you for health care decisions. Unfortunately, you are now on life support and your agent (your eldest child) is telling your doctors you have no desire to live this way. The doctors could say either themselves or their hospital has a policy not to take termination orders from an "agent." At that time your agent will present to the doctors your prepared advance directive telling the doctors in your own words you do not want to be prolonged by artificial means.

Personal Property – Often overlooked but very important

After thousands of reviews of estate plans probably one of the most overlooked items we run into is that most plans forget to transfer personal property into the trust or leave a detail letter or a letter of wishes to their loved ones. Most estate planners work hard to make sure your real estate, bank accounts and investments are transferred to your trust. However, sometimes they leave out the details of how your personal property will be owned going forward. The problem with this mistake is you could still end up in probate by way of your personal property. This is especially true if you own expensive personal property such as antiques, jewelry, art collections, guns, tools of a trade, or expensive equipment of hobbies.

All your hard work to get all your other assets in your trust to avoid probate will be for nothing if you forget this very important document called a, "Deed of Gift." A Deed of Gift is a court recognized document that says, "…all my personal property has been transferred to my trust." No need to go around the house placing little sticky notes on everything saying it's owned by the trust.

Last Will and Testament – Not all wills are alike

Most of you have probably prepared a Last Will to make sure that everyone knows how your assets will be distributed at your death. If you have not yet prepared this very important document, "shame on you." I am being overly dramatic here for affect but it's to prove my next point. If you have not prepared a will your state has statutes that determine who gets your assets. Do you want the state saying who gets your stuff? Not only will the state decide who gets your stuff but your loved ones will have to go through a judicial process called, "Probate" before anyone gets anything. Probate can be time consuming, expensive and aggravating.

So, if you have prepared your Last Will don't pat yourself on the back too soon. Even though you have done a great job at preparing for your final demise, you too will be putting your loved ones through probate. Sounds like someone is playing games with you, right? The results are the same in either case whether you have a will or not, your loved ones will go through probate. The difference is, if you have a will you decide who gets what.

Here is the difference in how wills work. If you just have a simple will your loved ones will have to probate the will. However, there is a different kind of will called a, "Pour-Over Will." The Pour-Over Will is used in conjunction with a trust. Therefore, your loved ones will not

have to probate this Pour-Over Will. The "Pour-Over" part of the name is just as it indicates. The will "pours over" into the trust any asset left outside of the trust at your death.

Another point must be made and that is a simple will becomes public record when it is recorded in the probate courts when you pass away. Once it is recorded it becomes a public record and anyone can snoop into your affairs by viewing the will at the courthouse or public records department. That's how we know how the estates of the movies stars and ultra wealthy are distributed. Some journalists know that they have to do is go to the proper public records office and ask to see the will. They then make notes and report what they found in the articles they write. By this same procedure so could anyone who wants to pry into your affairs or even make trouble for your estate by snooping into your personal affairs. A Pour-Over Will gives no detailed information about "who gets what." Again, that's how a simple will works.

However, a Pour-Over Will protects your privacy because we leave out the details of who gets what and who's the executor of your estate. Therefore, we are able to meet the requirements of the law by putting those necessary clauses in the will that require your executor to pay your final debts, file your final tax returns, take credits for prepaid taxes, use money from your trust to pay down debts and finalize your affairs. On the other hand, we provide you with a valid will, we make sure anything that was left out of trust is then poured over into trust at your death and we protect your privacy, all this is accomplished with the use of this Pour-Over Will.

Probate Explained

Many people have had differing opinions about how bad or how easy probate can be. However, I have heard many horror stories about probate, plus lessons learned from my own family many years ago when a great aunt passed away. Her estate was held up in probate by her quarreling siblings and eventually the family lost her house due to the extended period in which it took to close probate. My story is more indicative of a typical probate than some of the easy probates that I know do exist as well. Even in some cases where there are no relatives contesting the will even a simple non-contested probate could be aggravating, expensive and time consuming.

Probate is a judicial process (court proceeding) that oversees the distribution of assets of a deceased person. In most cases, the scenario

will follow pretty closely to the following example. Once your loved one passes away you will need to post their will in his/her local probate court or public records department. In some states this could even be filed in the family court system. Either way, most states require a will to be posted at the death of a resident of that state. Next, your loved one will have to hire an attorney to "probate" your will. Usually, the attorney will ask for a retainer to do the work of settling the estate. In most cases the retainer can be as little as $4,000 to as much as $20,000. Those numbers are just to start the process. If the probate process drags on for any length of time these numbers can and will most likely go up.

Continuing my scenario, a judge will be in charge of the proceedings. You have to get permission from the judge to do just about anything in the deceased person's estate. You can not take it upon yourself to give any articles of the deceased away without permission of the court. You cannot spend money from the accounts of the deceased without permission of the courts. Sometimes, the judge may ask you to post a bond before he/she (the judge) will appoint you as the executor, even though you were appointed in the will of the deceased person as his/her executor. The judge may also ask you to provide accountings to the court, meaning you will have to show the books of a business and/or the bank and investment account statements to the judge either monthly or quarterly depending on the judge's order.

The next order of business for the executor is to get appraisals for any articles of significant value. For example, I once had a friend whose father passed away. Her father's hobby was building custom Harley Davidson type motorcycles. He was in the process of building three when he passed away. He also, owned a vacation home on Cape Cod along with his primary home in New Hampshire. He also owned two cars and a truck. Needless to say, my friend had to find appraisers, schedule the appraisal and pay the $300 to $400 price for each appraisal. Add those costs to her time off from work, travel to and from another state, attorney fees and court cost.

So far, I have given examples of what the executor must do to further along this probate process and to complete it as soon as possible. Here are some things that are not the problem of the judge or the executor. It's just a general problem of probate. Here's what I mean, say that the will calls for the estate to pay every child of the deceased person 25% of the total estate and there are four children of the deceased. Sometimes this is not a problem for the children. However, sometimes this could be a big problem. Say for example, one of the children is going through a divorce or is being sued. The money that would have gone to him as an inheritance will most likely be swallowed up by his soon-to-be ex-spouse or the party suing him.

Here's another example, what if one of the children had a drinking problem or a problem with substance abuse. A large inheritance could be a problem in the hands of an addict. This is a problem of probate because probate has a rule that requires the executor to deliver the inheritance as ordered by the will regardless of the present situation with the children inheriting the assets of the deceased. If the deceased has not already anticipated these problems and did not prepare for them in his will, the results could be devastating.

My next example deals with the inheritance of children who predecease their parents. In the case where a child dies before the parents but the parents never updated the will or included provisions in the will for such a scenario, parent could conceivably disinherit their grandchildren accidently. It's common for most attorneys to include such provisions. However, it's also not uncommon to see wills that really don't do a good job at handling these types of scenarios. Here's a real life example, say your child dies before you but you haven't changed your will to handle the death of your child. Say also your child has minor children. In the event of your death those grandchildren will most likely take the share their parent would have taken had the parent survived you. Under this scenario your grandchildren are minors and can not handle their inheritance by themselves. Therefore, usually the surviving parent (your widowed daughter-in-law) will be in charge of the inheritance money. That's okay as long as no other parties enter the picture.

However, let's see what happens when another party enters the picture, say for instance a new husband for your son's widow. That new marriage only last two years and ends in divorce. In most states your son's widow will have to provide financial disclosers of all her finances to a family court judge. It's completely up to the judge to decide how to split the finances between the divorcing couple. In most states the judge will have to, by law, take "all finances" into consideration when he/she divides the assets between the divorcing couple. Here's my point, if you like your grandchildren you probably don't want to disinherit them accidently. However, in some cases probate could actually have this result.

I have given this same talk in many seminars to many people. Invariably someone would come up at the end of the seminar to tell me about their very easy probate experience. I always congratulate them on their good fortune and remind them that my scenarios are more about what could go wrong and not that every probate is a nightmare. If we have the advantage of planning before hand we can do a better job at avoiding this possible disaster. Why put your loved ones through this

outdated, time consuming, aggravating and wealth reducing process, if it can be avoided. Your next question should be, "How do we avoid it?" I thought you'd never ask! We avoid probate, spell out in detail who gets what, protect your privacy, protect assets for your children and at the same time we won't change the way you live your life. Our solution is a revocable trust. I will explain how they work next.

Revocable Trust – How they work

Back in the mid 90's when I first started in the business of estate planning I was an investment advisor at the time. I worked with local attorneys to provide the necessary legal documents for my clients to build their estate plans. However, back in those days when my clients would try to do business with the local banks or other investment institutions, the fact that they were doing business as a trust seemed to throw everyone for a loop. I had a client once call me crying from the bank lobby upset that the banker wouldn't allow her to register her accounts in the name of her trust. At the time not many people had even heard of a revocable trust. If they had heard of them they were always under the impression that these trusts were reserved for the ultra wealthy. That was almost twenty years ago and *my have times changed*. Now banks, investment institutions and mortgage companies don't shy away from doing business with trusts anymore.

A simple revocable trust is a mechanism that allows the "Grantors" (the clients) to put their assets in trust for the benefit of some third party, usually their children. There's a third component to that first sentence and that is there has to be a trustee (person in charge) to control the assets of the trust. During the grantors lifetime they are both the current trustees and beneficiaries, meaning they can do whatever they want with the assets of the trust. It's not until both grantors have died that the future beneficiaries are able to takeover the trust. At that point the once revocable trust now becomes irrevocable and the provisions of the trust dictate how things will be distributed.

Who Needs a Trust

Let's back up for a minute. Why would anyone need a trust? That's a trick question to see if you're paying attention. There are many reasons for establishing a trust. I would literally get upset when I hear clients tell me that their other attorney said they didn't need a trust because their net worth was below some arbitrary dollar figure. The reason this would upset me is because there are more reasons than just money to form a trust. For example, a person of even modest wealth

($200,000 to $400,000 in liquid assets and a house) who happens to be in a second marriage and have children from the prior marriage may be a prime candidate for a trust. Let's play out the scenario. Bill is married to Sue. Bill has two children from his first wife. Bill's children are both adults with families of their own. Bill is still very close to his children and the children get along great with Bill's new wife.

Now if Bill were to suddenly pass away without a trust or a will this would most likely start a fight between the children and the new wife. The reason being the children would probably expect something from their father while the new wife will probably expect that everything should go to her as the widow. Bill and the new wife had prior conversations that should anything happen to Bill the wife would get everything, then at her passing whatever is left will go to the children. I have seen this many times in my practice. However, what no one realizes is that there are all sorts of problems with this plan. There are some states that say the children are entitled to some share at their father's death. There are some states that determine what the wife can demand for herself. What will most likely result will be a long drawn out probate of the estate. After the lawyers are paid, all the time missed from work and the divide created between the family, the estate would be devastated financially and the family dynamic will be destroyed. Even with other attorney's good intentions, the advice of should you have a trust or not doesn't have as much to do with money as you would think.

Other reasons to establish a trust could be: to spell out who gets what, when, how, and where when you die; to plan for charitable contributions; to divide estates between children from a prior marriage to be shared with children from the current marriage; to provide for future beneficiaries for many generations; to protect children and grandchildren's assets from being absconded by divorce, litigation, creditors and attachments. Trusts are particularly good at avoiding fighting if there is already discord among family members. A well crafted trust will keep the family out of court by avoiding that forum for debate called, "Probate." I could probably come up with ten more scenarios of why people need trusts but for now if you don't have any of the above mentioned issues just think of a trust as being a way for just ordinary people to prepare for an orderly distribution of their assets at their deaths.

Ownership is the Key

Practically speaking, most of us own our things in our own name. For example your house, car, bank account, investment accounts are all listed in your name. If you are married some or all of these items may be in both your names. Either way, my point is that the actual ownership is with you the individual or you and your spouse as the joint owners. As long as these accounts are in your name they will eventually have to go through probate to get them to the next generation. If you own things jointly then the survivor will inherit the balance of the asset at the death of the first person to die. At this point if things are owned jointly there is no probate. However, when the survivor dies the account has to be probated to go to anyone else.

How Self-help could cost you more than legal fees

Now I know some of you like to self help so you run out and put your children on your accounts as joint owners, right? Wrong! That's a disaster waiting to happen. Here's why I say that. If you put your children on your accounts their liability becomes your liability, and vise versa. If they get in an accident and are found to be at fault and the claims exceed their insurance policy's limits the litigators are coming after their assets and if you share those assets they can be attached and you could lose what you have because of a false sense of protection.

Another reason you don't want to put your children on your title is for tax reasons. For example, if you own real estate and you want to avoid probate so you put your children on your real estate title there could be severe tax consequences of doing this. Here's what I mean, there is a concept called, "Step-up in basis." This concept is a credit that your children can claim if they inherit your property by way of a will or trust. However, if they are on the title with you prior to your death they will have to claim capital gains when they sell the property.

Being penny wise could make you pound foolish. For example, John doesn't want to pay a lawyer for estate planning help so he hears that if he puts his son, Mike, on his title that will avoid probate. John is right so far but here's where things go wrong. John bought this property twenty-five years ago for $100,000. Now the property is worth $250,000. John has had conversations with his son that goes something like this… "When I die son I want you to sell the house and split the money with your siblings." Mike's dedication to his father and love for his brothers and sisters will ensure that he does the right thing. If he does, that eliminates one of the problems with this scenario.

John dies soon after that conversation. Mike sells the house for $250,000. Mike later consults with his accountant about the sale of the

house and low and behold the account informs Mike that he is responsible for a huge capital gain tax. Mike realized a $150,000 capital gain when he sold the house. Mike's tax bracket will put him in a 15% capital gain rate. The result of John's self-help is a tax bill to his children to the tune of $22,500.

Competent estate planning would have eliminated this problem by putting the house in a will or a trust to give the children a free step-up in basis. Meaning they would not have the tax burden that John created with his self-help method.

Getting back to the topic of trusts, here's how the trust would have eliminated the tax problem mentioned in the example above. When we transfer real estate to a trust the trust will pass the property to the beneficiaries capital gains tax free, regardless of how big or small the actual gain is.

Owning things in the name of your trust

As we started this topic talking about how we own things in our own name. I mentioned the usual things that we put in our names such as our cars, house deed, bank accounts, etc. The way that these items are titled causes a probate problem. When we own things individually they have to go through probate to get to those people whom we would like to have our stuff when we pass away. Therefore, the simple solution then would be to get these things out of our name. But not just putting them in joint ownership will help. You would have to keep adding joint owners every time someone dies.

Some banks and investment institutions allow you to designate a "pay on death" beneficiary. This can be a great help to someone who does not have a trust. However, remember that at the death of the primary owner it becomes the new property of the pay on death beneficiary. Remember in some cases an outright distribution may not be the best thing at any given time for a beneficiary. The simple solution is to transfer the ownership to your Trust. Every single state within our United States has a law that says assets owned in a revocable trust do not have to go through probate.

Funding your trust

When you establish a trust it's like creating a separate person (fictitious entity) to care for your assets. The trust is a legal entity that can hold assets, transact business, distribute to beneficiaries and a whole host of additional controls and benefits. Once the trust is established we then start the homework portion of funding the trust. Funding is where we work with you to get all your assets in the name of the trust.

One of my biggest pet peeves when I review estate plans is that in some cases the funding is not complete. This could have disastrous results for a family who established a trust in hopes of avoiding probate only to have to go through probate anyway because funding was incomplete. Therefore, we follow a funding checklist to complete before we can say that we have completed the process of establishing a comprehensive estate plan.

I give my clients a checklist of items that they must complete to complete funding. These items are simple tasks but must be done. For example, the list will have instructions on how to change your bank account to the name of your trust. It will have instructions on how to change your beneficiary designation on your insurance policies, 401(k)'s and IRA's. If you are doing planning or have already established an estate plan, check with your estate planner to see if you have completed your funding.

Everything you own including real estate, bank accounts, investment accounts, etc. should be transferred to your trust. If you get nothing else out of these writings this piece of information is crucial. If you have successfully completed funding you are assured your loved ones will not have to go through probate.

Follow up and Review

I once had a couple come to my office for a review of their estate plan. I looked at the trust and it looked good. I combed through all the documents with a fine tooth comb. I have reviewed over a thousand trusts in my career and this one was one of the better estate plans that I had ever seen. The law firm was a prominent firm out of Hartford, Connecticut. I told the couple that based on our conversation the trust does everything that they wanted in there estate plan. All the provisions were up to the current laws at the time. All the provisions for their children were included. There was no arbitrary language or ambiguities. The documents were even enclosed in a beautiful binder. Everything as I said looked good.

To my surprise the couple looked disappointed and said, "…well we still want you to be our attorney." I was surprised because there was nothing more I could do for them. I asked, "…why would you leave a firm who had done such good work for you." They said that every time they had a question or needed a copy of their documents they would get a bill.

The husband said he once needed a simple question answered about their real estate holdings. The attorney spent 20 minutes talking about his golf outing the day prior to the phone call and only about 10 minutes answering the client's real estate question. You know where I'm going here, you guessed it, a week later the client received a bill for a half hour legal fee in the mail. My point is this… it's one thing to do good work but you have to have a firm that's not going to nickel and dime you on the reviews and follow up.

Remember these are revocable trusts, meaning as your life changes so should your estate plan. In some case people pass away and we have to change your estate plan to reflect that death. In other cases people move away and are no longer available as a power of attorney agent. Things change in our lives over time. You should be comfortable with calling your attorney to have them update your estate plan without fear of a huge bill. Now, I am not saying you should expect all your updates to be free. But a reasonable fee for good service should be expected.

As for my firm, we don't charge for phone calls, quick answers and copies. However, what we would charge for are extensive rewrites or revisions. If it's going to take a couple of hours are more to do the work, then you will probably get a bill. Otherwise, we will review your plan about every 3 to 5 years, or so, unless something happens in your life and you need to see us sooner.

Every now and then the laws will change regarding trusts, taxes, powers of attorney, etc. As a result we will contact our clients to let them know when the changes will affect them. We have only had a couple of big changes in the last ten years.

Summary

Basic Estate Plan

Basic Pour-Over Wills

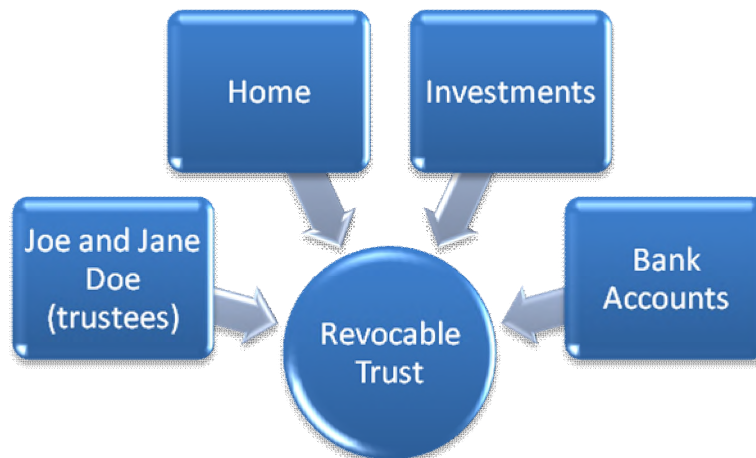
protects privacy and points to trust

Durable Powers of Attorney

for administration and financial matters

Health Care Powers of Attorney

to make health care decisions for each other



Here we have a basic estate plan. It includes a Pour-Over Will. This is just like any other will with the exception that it is vague on its face purposely. We purposely make it vague because once posted in the probate court's office this will becomes public. That means anyone with prying eyes can request a copy and see who gets what and who's in charge. We protect your privacy by not revealing any of that vital information in the document.

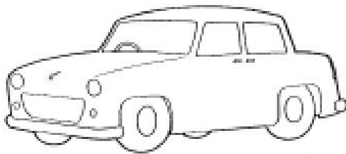
Next we have the, all important, Powers of Attorney. These are set up early so that when they are needed no one has to go to court and petition for guardianship over your loved ones affairs. With these powers of attorney in place your agents can step in right away to make medical decisions and/or handle financial affairs.

Most of us own things in our name. Either we own them individually or in joint ownership with our spouse.

Harry and Sally

Bank Accounts

Retirement Accounts



Automobiles

Houses

Our personal Property: Jewelry, Antiques, Art Collection Expensive Tools and Equipment, Guns and Coin Collections

The key to avoiding probate is changing the way we own our things. If we transfer ownership to a revocable trust State Laws say we don't have to probate these items.