TRUSTS

REVOCABLE "LIVING" TRUSTS : Allows for an appointed trustee with the power to transfer all assets held by the trust to those persons designated to receive them.

Due to the high statutory fees on some of the simpler methods of, people began trying to reduce the cost of transferring assets at death. One very common method is through the use of revocable *inter vivos* trust, commonly called Living Trust. These trusts appoint a trustee (usually a family member) and give the trustee the power to transfer all assets held by the trust to those persons designated to receive them within the document. This transfer usually happens at the death of all the person(s) creating the trust. Thus, the need for court ordered transfer is not required. However, court jurisdiction is optional at the request of any person involved in the trust.

A/B TYPE LIVING TRUST

In order to avoid wasting one spouse's unified credit, the A/B type Living Trust was created. It requires an allocation of assets between two newly created trusts within the original Living Trust.

Per the terms of this trust, a survivor's trust and a bypass trust are created at the first spouse's death. Allowing one unified credit to be applied to each trust at its owners (each spouse's) death and both spouses credit's get used.

The surviving spouse has unrestricted control over their surviving trust's assets and some restrictions apply over the use of the bypass trust's assets during the surviving spouse's lifetime. Yet the surviving spouse usually receives an unlimited right to income from the bypass trust's assets, until death. The net effect is the ability to shelter up to twice the unified credit amount in assets from Federal estate and gift taxes by using both spouses' unified estate and gift tax credit.

Other variations on the A\B type trust add additional trusts to the original trust mix at one spouse's death, but they function basically the same. They are, most times, used to assure that the separate property of one spouse goes to the children of that spouse from a prior marriage.

My preference is to use a Disclaimer Trust, rather than an A\B Type Living Trust, that allows the surviving spouse the option of creating or not the A/B Type Living Trust if it is needed for tax purposes at the death of the first spouse. This allows maximum flexibility to the surviving spouse at the time when the taxes are due.

At the first spouse's death there are attorney services required to remove the decedent's name from title to assets in which they appear as a co-trustee and creating the additional trust. At the second death, there are statutory requirements imposed upon the successor trustee prior to any estate distribution. Even with both of the above services performed, it usually does not come close to the cost of probate for most estates.

CHARITABLE REMAINDER TRUST

This type trust is an important vehicle for dealing with highly appreciated property having a low tax basis that if sold, would create substantial capital gains for the seller(s). This trust is created, and the appreciated asset transferred to the trust *then* the trustee sells the asset and invests the proceeds in income generating assets.

The property donor receives the following:

• a stream of income from the trust for a term of years or until death is paid to the creator.

• avoids the high capital gains taxes and receives a tax deduction (although less than dollar for dollar)

• at the end of the income stream, the charity receives the assets remaining in the trust.

Many people couple this trust with a wealth replacement trust –to replace the wealth given to the charity.

CHARITABLE LEAD TRUST

This trust pays the stream of income to a charity for a term of years, ~~and~~ then the assets remaining *in the* trust go to your heirs after the term of years has ended.

Due to the term of years that the heirs must wait to receive full use and enjoyment of their gift, the value of the gift you gave them is discounted and the gift tax liability you owe is thereby reduced. Your heirs receive the original gift's value plus its appreciation and income, less the income stream designated to be given the charity.

GRANTOR RETAINED ANNUITY TRUST

The Trust creator would take an income stream for a term of years from the investment placed into the trust. After the term of years has terminated, the then existing investment including its appreciation and income less the income stream you took over the years, goes to your heirs.

The appreciation escapes estate and gift tax during the term of years. The gift tax liability resulting from your gift to the trust is discounted due to the term of years your heirs must wait to receive the asset.

There is one catch, the person taking the income from the trust must live through the income stream term of years or the estate is placed in the same position it would have been had the trust not been setup for estate and gift tax purposes.

PERSONAL RESIDENCE TRUST

This trust is used to hold appreciated second homes with high capital gains attached to any sale of them. The home is placed in the trust for a term of years, then the gift is discounted due to the term of years that the heirs must wait to enjoy the asset. The heirs get the asset at its then existing value after the term of years has run. The value includes all appreciation resulting the duration of the term of years. Your estate is liable for the resulting gift tax on a discounted gift of the house. As with the Grantor Retained Annuity Trust, you must live for the term of years or your estate is placed back in the position it would have been had the trust not been created.

LIFE INSURANCE TRUST

This trust is referred to as a **Wealth Replacement Trust** when coupled with the Charitable Remainder Trust and life insurance policy.

The principal behind this trust is to purchase a new life insurance policy payable to the trust (or to transfer an existing life insurance policy) and remove the policy's proceeds from your estate for tax purposes, while having the proceeds available to your family.

If a large amount of insurance proceeds were thrown on top of your estate, your estate may not have the ability to shelter the larger amount from estate and gift taxes under your current plan. If an existing policy is transferred to the trust, the insured must live 3 years after the gift to the trust in order for the gift to be treated as outside the owner's estate for tax purposes. The policy premiums are paid by the trustee from gifts using your $13,000.00 annual gift tax exclusion made to the trust. The policy payout amount replaces the asset given to charity or adds additional wealth to your family allowing any investment income to flow to the surviving spouse for their life and the remaining balance to be given to your children after both spouses' deaths. Married couples usually select a 'second to die' policy to reduce premiums. This can also be used in the same fashion by single individuals to provide additional wealth to their children.

The one drawback is that in order for the gifts to qualify for the $13,000.00 annual gift exclusion, the children must possess the present ability to withdraw the gifts designated to pay premiums each year as they are made to the trust. To the extent the children do not withdraw the money, this plan works very well.

For more information on the various types of Trusts, please contact me to go over your particular situation and needs.

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