Welcome! What's your local institution?

- Langston University
- Oklahoma State University

Prepare Your Estate Plan: Print this Lesson

Last Updated: August 18, 2008

This page contains the entire *Prepare Your Estate Plan* lesson to make it easier for you to print the lesson contents. For best results, view and print the lesson using the Internet Explorer browser.

Return to the Prepare Your Estate Plan learning lesson.

1. Prepare Your Estate Plan -- Introduction

How will your assets be distributed upon your death? Have you prepared for the distribution of your estate for the loved ones you will leave behind? Perhaps you have made plans to distribute your estate, and they need to be reviewed and updated. In any case, you can proceed through this lesson and learn more.

This lesson has unique sections that lead you through the learning process and can be viewed sequentially or in a random order. Select a unit to view from the "Lesson Contents" list on the right. You can also progress through the lesson by clicking the "Next" or "Previous" links at the bottom of each page.

Use the case studies in this lesson to apply what you have learned. For definitions of terms used in this lesson, go to the Financial Security Glossary.

IMPORTANT NOTE: The information on this Website is not legal advice. The information in this lesson will provide general information and help to make you a better informed consumer of legal services. It is designed to help families become better acquainted with some of the concepts and tools used in estate planning and to create an awareness of the need for such planning. Laws vary dramatically from state to state, and future changes in laws cannot be predicted. The statements within this lesson, facts sheets, and learning activities are based on general concepts as of the last revised date of the Web publication. If you have questions, you should seek the assistance of an attorney in your state, who can give you advice based on local laws and your facts and circumstances.

1.a. Lesson Objectives

In this lesson you will:

- Learn what is included in an estate plan
- Gain a basic understanding of estate-planning tools:

- Power of Attorney
- Property Ownership
- Wills
- Probate
- Estate Taxes/Gifts
- Trusts

- Receive suggestions for hiring and working with an attorney
- Increase your knowledge by reviewing several case studies

Have you put off making plans to distribute your property when you die?

There are many financial and emotional reasons for having an estate plan. Just think about the suffering and expense family and loved ones could be spared if plans are made in advance. Now is the time to get started! If you already have a plan, this lesson will help you review or modify it, if necessary.

An AARP survey (2000) about the general use of estate-planning tools found that among Americans age 50 and older:

- 60% had a will
- 45% had a durable power of attorney
- 23% had created a living trust
- 36% had none of these legal documents
- 17% had a will, durable power of attorney, and living trust

2. Planning for Your Estate

Estate planning is arranging for the orderly transfer of your property and resources to other people during life and after death. Your estate is essentially everything that you own. Your property and resources can be transferred through beneficiaries identified in documents (i.e., pensions and life insurance policies), wills, trusts, gifts, and joint ownership of property—all of which can be part of an estate plan.

Since you may accumulate many resources during your lifetime, you will probably want to decide to whom you wish to transfer your possessions upon your death. Everyone needs an estate plan. If you do nothing, the state will decide through state law how to transfer your property after your death.

How would you answer the following questions?

If I were to die tomorrow…

- Who would get my property?
- Who would care for minor children, parents, and/ or a spouse?
- Would the family business continue?
- Would the estate be settled according to my wishes?
- Would taxes, fees, and costs be held to a minimum?
- Would a trust have been appropriate for me?
- Would my estate be settled in an appropriate and timely manner?

Plan to have your wishes carried out by taking action to develop an estate plan now.

3. Power of Attorney: Planning for Incapacity

A durable power of attorney for financial matters is an effective way to arrange the handling of your business and personal affairs if you become unable to do so.

Our ability to handle financial affairs can be diminished by degenerative diseases such as Alzheimer's, dementia, or serious accidents. It can happen to the young or the elderly. We never know if or when tragedy might strike.

A durable power of attorney is a simple, inexpensive, and reliable way to arrange for the handling of your financial affairs. It allows the designated person to pay bills and file taxes in addition to handling other financial matters. Both a durable power of attorney for health care and a durable power of attorney for finances are needed.

3.a. Common Types of Powers of Attorney

Power of Attorney: This document is commonly known as a financial power of attorney and gives one person (the agent) authority to act on behalf of another person (the principal). Full power or limited power can be granted in the document.

Attorney-in-fact: A person who is given authority by a power of attorney; sometimes called an agent. This person does not have to be a lawyer. It could be your spouse, an adult child, or close friend.

Durable Power of Attorney: While similar to a general power of attorney, a durable power of attorney continues after a person becomes disabled, incapacitated, or incompetent. This is a time when the power is most needed. In most states, it must be signed and notarized to indicate that it is "durable." *(Note: Many states require that a power of attorney contain specific words to create a durable power of attorney. Consult an attorney to see what language must be included to create a durable power of attorney in your state.)* It permits the person you appoint to handle your financial affairs and can be flexible by allowing the agent as many powers or as few powers as you wish.

Springing Durable Power of Attorney: The power-of-attorney document can specify when the document goes into effect. If it specifies that a doctor must certify that you have become incapacitated in order for it to take effect, it is called a "springing" durable power of attorney and allows you to remain in control of your financial affairs until you become incapacitated. Note that it cannot take effect unless it is “durable.” *(Caution: Today's medical privacy laws have made it difficult or impossible for doctors to sign statements that patients are mentally or physically incapable of managing their personal affairs. Unless the condition that “springs” the power of attorney into effect is specified in the document, it will be defined by state law.)*

3.b. Duties of and Selection Criteria for the Attorney-in-Fact

Duties of the Power of Attorney: A power of attorney gives a broad range of business and financial powers as specified in the document. Some typical powers in a very broad power of attorney might include powers to:

- Do many personal business transactions or other acts that you could otherwise do
- Sue in your name and collect money owed you from any source
- Make gifts of real or personal property
- Buy or sell property (of any type) owned in your name
- Maintain, improve, rent, or lease any of your property
- Establish or terminate any financial accounts in your name
- Sign any contract in your name
- Sign your name to any tax returns

A power of attorney can be either full or limited as outlined in the legal document. There are some things that the holder of a power of attorney cannot do on your behalf; these include:

- Fulfilling a contract that requires your personal services
- Completing a legal affidavit that requires your personal knowledge
- Making a will for you
- Voting in an election for you

A power of attorney becomes void upon the signer's death.

Selection Criteria for the Attorney-in-Fact: Choose your agent carefully. You are giving this individual the power to perform important financial transactions outlined in the legal document. If given full power, your financial agent/attorney-in-fact can transfer assets into a trust while you are alive and do anything that you could do, if you were still able.

- Your agent—or agents—may be a relative or friend, or you may want to hire an accountant, trust officer, or banker.
- For convenience, it is helpful if your agent lives in close proximity to you.
- Choose a person who is trustworthy, has good financial management skills, and has earned your utmost confidence in his or her judgment and ability.
- Because handling the financial affairs of another can be a time-consuming job, be certain that the person you designate is willing to take on the responsibilities, if necessary.

If you become unable to make your own decisions and have not prepared this document, it is likely that your family will have to seek a guardianship or conservatorship action from the court in order to have the legal authority to manage your financial affairs. This can be inconvenient, costly, and cause delays. This is an important document; don't delay in getting it prepared.

4. Property Transfer: Documents and Legal Arrangements

Several tools and planning options are available to ensure that your money, possessions, and real estate are passed on as you would like. All of these legal arrangements have advantages and disadvantages. Use of one or a combination of these tools will be based on your circumstances, your wishes, and the way in which you want to protect your loved ones after death.

Beneficiary Designation: Some assets pass by means other than a will; these include insurance policies, Individual Retirement Accounts, 401(k) plans, pension plans, and profit-sharing plans. Beneficiaries and payable-on-death (POD) or transferable-on-death (TOD) designations are named on the contract, and—unless you designate "my estate" or make no choice at all—the transfer takes place directly upon death without involving the probate court. You can change your beneficiaries as the need arises by completing the required paperwork with the account holder—a bank or brokerage company. You cannot change them using a will or other estate-planning method. It is important to review beneficiary designations annually or when circumstances change to make sure that your assets will be distributed as you desire.

Gifts: Gifts are voluntary transfers of property without receiving payment before you die. Examples include stocks, cash, real estate, equipment, and personal property. Gifts can reduce the size of your taxable estate. However, if deathbed gifts leave the estate without funds to pay creditors, the probate court can order the property to be paid back to the estate. Gifting law is complex. Gifts can have an impact on taxes and eligibility for public benefits such as Medicaid to pay for nursing home care. Consult experts before making any substantial gifts.

Property Ownership: Property ownership involves tangible, intangible, and real property (possessions) to which its owner has legal title. The way in which you own property or the way it is titled (such as single or joint ownership) will determine how it is distributed upon death. Moreover, ownership is defined by state laws. It is important to make wise decisions about how property will be transferred to insure that it gets to the intended party. Careful consideration in planning and titling property will help avoid unintended consequences.

Will: A will serves as a written document that provides instructions on how you want your assets distributed after your death. It is often the easiest and least expensive estate-planning document to prepare. Also, it will permit you to name a guardian for your minor children. The main disadvantage of a will is that it must go through the probate process when you die. There are costs and delays associated with probate, which vary widely from state to state. Consult an attorney to determine the impact of probate in your state.

Probate: Probate is a court-supervised legal process that proves the validity of a will and oversees the administration of an estate with or without a will. It involves the procedure of gathering the decedent's assets; paying debts, taxes, and expenses of the administration, and distributing assets to the heirs or beneficiaries of your estate.

Trust: Assets can be transferred through a trust. When you transfer property to a trust you have created, you make a gift to the beneficiaries of that trust. Trusts can help avoid expenses and time involved in the probate process, and can help eliminate and reduce estate taxes. Assets in a trust can also be managed and distributed according to a predetermined schedule.

4.a. Property Ownership

When you begin estate planning, it is important to understand property and the property rights associated with its ownership. The form of property ownership has an important impact on the degree of control during life, as well as how property will be taxed and distributed after death.

All estates are made up of property. It may be tangible property, intangible property, real property, or a combination of the three.

Tangible personal property is property that can be touched or felt, such as cars, stereo equipment, television sets, furniture, silver, china, clothing, or furs. Tangible personal property is often called personal effects or household goods.

Intangible personal property might include stock certificates, bond certificates, patents, trademarks, or copyrights. Cash, checking accounts, savings accounts, money market accounts, and certificates of deposit (often referred to as liquid assets) are also part of your property.

Real property is real estate and land and anything that is affixed or erected upon the land. It can include fences, barns, mineral or oil rights, and crops or timber, to name a few.

4.b. How Property is Titled

There are several ways you may own real and personal property. The way in which you own property will determine what part of it—if any—you may give away. Moreover, state law defines the types of ownership. If you own property (i.e., real estate) in another state, the laws of that state will apply. For personal property, the laws of the state in which you claim residency will apply.

Joint ownership is a popular way to leave property to loved ones; however, it is not always the best way. There are advantages and disadvantages to joint ownership in an estate plan. In general, the primary advantage of owning property jointly is that your property passes automatically to the surviving joint tenant(s) when you die and probate is avoided. One disadvantage to joint ownership is that the decision is irrevocable unless you get the permission of the joint tenant(s). Another is that, in many instances, you have made a taxable gift to that person or those persons.

An exception to the rule of joint ownership is when adding a joint tenant to a bank account. Adding a person's name to your account is not an irrevocable decision indicating that you made a gift to that person. It is, however, a decision to take seriously, as the person can withdraw all of the money from your account. It is important to check with the financial institution to determine the rights created when you add a person as a joint tenant to a bank account.

See Prepare Your Estate Plan Case Study 3: The Dangers of Making Someone a Co-owner of a Bank Account as Joint Tenants with Right of Survivorship

4.c. Types of Joint Ownership

Several types of joint ownership are described below:

Community Property: The laws of some states specify that most property acquired by either spouse during a marriage is held equally by husband and wife as community property. Laws in a community property state provide that any property purchased or salary earned by a married couple during the course of their marriage is owned equally by each.

Joint Tenancy with Rights of Survivorship: This type of joint ownership states that, upon death, an owner’s share goes to the other joint owner. Joint tenancy is created when two or more persons purchase or are given property at the same time. Each joint tenant owns an undivided interest in the whole property, and each has the right to possess, occupy, enjoy, use, or rent the property. The right of survivorship means that upon the death of one of the joint tenants, by law, the property automatically belongs to the surviving tenant and does not pass through probate. Therefore, upon the death of a tenant, property held by joint tenancy with rights of survivorship cannot be transferred or given away by a will.

Tenancy-In-Common: Ownership of property in which, upon death, each owner’s share goes to his/her heirs or beneficiaries is known as Tenancy-In-Common. It is created when two or more persons own property together but also own separate titles to the property. Property owners may or may not own the same percentage of the property. For example, one may own 25% while the other owns 75%. Each owner may do as he or she wishes with his or her interest in the property, such as give it away, sell it, or mortgage it without the consent or knowledge of the other owner. With tenancy-in-common, upon death, one person’s share passes as provided in his or her will or trust. Probate or other consequences are possible.

Tenancy-By-The-Entirety: This form of joint tenancy between a husband and wife is valid in a few states. Tenancy-by-the-entirety provides extra protections to real property owned by a married couple. One spouse owning property as tenants-by-the-entirety cannot mortgage, transfer, or otherwise deal with the property in any way that would affect the rights of the other spouse without the latter’s consent. When one spouse dies, the other still owns the entire property.

There are some important things to consider about joint tenancy:

- Joint tenancy can have some advantages over other ways of transferring property, but there are dangers and unintended consequences. It is wise to check with a lawyer before entering into an agreement.
- Generally speaking, if you have doubts about your co-owner, avoid joint-tenancy agreements.
- If you are over the tax threshold, joint-tenancy agreements can cause real problems by transferring ownership to the wrong co-owner or making it harder to transfer property to minimize taxes. If the gross value of your estate is likely to exceed $1 million at the time of your death, it is a good idea to seek expert tax advice. With increasing real estate

values, this amount is becoming more and more common.

- Coordinate joint tenancies with your will, trust, or other parts of your estate plan. You need a will and/or trust with a joint-tenancy agreement; it is not a substitute for a will.

5. A Will: Who Needs One?

A will is an estate-planning tool that serves as your set of instructions regarding who gets your property and resources when you die. At a minimum, everyone needs a simple will. It is the document that most people use for transferring their property, and it is often the choice of young families and of others whose situations involve neither complex tax planning nor resource management for incapacitated family members. After death, the will is settled through the probate process.

To appreciate the terminology used in a will, select Prepare Your Estate Plan Case Study 4: How Much Will Each Heir Inherit? Remember to access the Financial Security Glossary for an understanding of the terms used.

Why have a will?

- It allows you to decide how to distribute your assets after death.
- It lets your wishes—rather than state law—determine how to distribute your resources to your heirs.
- It allows you to appoint a guardian of your choice for minor children.
- It allows you to name important people (an executor/executrix or personal representative) who will carry out your wishes.

5.a. What Constitutes a Valid Will?

Factors that must be present in a valid will vary from state to state, so it is wise to check your own state's requirements. Certain elements are often necessary:

- *Legal age:* You must meet your state's age requirements to make a will. Some states have exceptions for married minors and parents.
- *Sound mind:* You must know that you are making a will, how much property you have, and the names of the descendents or relatives who should share in your estate.
- *Intention to transfer property:* You must have a statement intentionally leaving some or all of your property to specific persons or entities.
- *Written:* Your will must be written.
- *Properly signed:* You must voluntarily sign your will, unless unusual circumstances such as illiteracy, illness, or accident prompt your lawyer to make alternative provisions.
- *Properly witnessed:* In most states, the signing of a formal will must be witnessed by at least two adults who understand that they are witnessing, are competent to testify in court, and are not receiving anything through the will.
- *Properly executed:* Your will must include a statement attesting that it is your will and a date and place of signing. It must be signed before witnesses in your presence and certify that all parties watched each other sign the document.

5.b. Types of Wills

There are several types of wills:

Attested wills are the most common type of wills. An attested will is usually prepared by a lawyer in typewritten form and signed in front of several witnesses who have no benefit in the will. All of the witnesses must sign it in front of one another and in front of the person making the will. The will-maker must also sign it in front of all of the witnesses. All of the previously mentioned signatures occur at one time in the same place.

Holographic wills are hand-written wills. State laws vary regarding their validity. Holographic wills must be signed by the writer and are unwitnessed. They are often ambiguous or defective and may cause delay, expense, and litigation. It is wise to consult an attorney before writing your own will.

Oral wills are also called nuncupative wills. An oral will is spoken and not written down. Only permitted by a few states, oral wills are typically made during a last illness and for personal property that is small in value.

Self-proving affidavits or *self-proving wills* are legal in some states. A self-proving will is one that has been properly notarized and includes certification by the notary that it was properly signed by the witnesses and testator (will-maker). A self-proving affidavit serves as testimony, thereby avoiding the delay and expense associated with locating witnesses at the time of probate.

5.c. Will Kits and Forms

A will is not a good do-it-yourself project. The cost of working around a minor mistake in a will can far exceed the cost of having a will properly prepared by an attorney.

Nevertheless, will kits and forms are widely available on the Internet, in bookstores, office supply stores, and other places. People can be attracted to these products by their apparent simplicity and low cost, but it's important to use them with caution. Always have an attorney review any will that you prepare yourself.

Some disadvantages of generic will kits and forms:

- Some situations are more complicated and may require an attorney's expertise.
- Materials are often condensed and simplified, leaving out details for unusual situations.
- Materials are written to cover laws for an entire nation but cannot cover every jurisdiction.
- Laws are constantly being revised and may require a different form of information
- The legal requirements for a valid will can be arcane and very difficult to follow. One minor deviation from what your state requires can invalidate the entire will.

To understand the importance of getting legal help in writing a will, see Prepare Your Estate Plan Case Study 5: The Disadvantages of Writing Your Own Will.

5.d. Assets in a Will

Assets in a will, such as property, can be listed simply or detailed. They may include such non-titled property as family heirlooms and keepsakes, which have much more sentimental than financial value. Oftentimes, distributing family heirlooms and keepsakes presents greater challenges for family members than transferring titled property.

It is important to learn your state's laws regarding non-titled property transfer. The law varies widely from state to state on what is required to make wishes regarding personal property binding on the heirs of an estate. If you anticipate disputes over who gets what, talk to an attorney in your state to find out what you need to do to properly plan for personal property in your state. What worked for a loved one in another state may not work for you.

For ideas on discussing the distribution of non-titled property with sentimental value, see "Who Gets Grandma's Yellow Pie Plate?" http://www.yellowpieplate.umn.edu/indexB.html

Remember that some assets with beneficiaries—which may include life insurance policies, pension funds, and Individual Retirement Accounts—pass outside of a will.

5.e. Changing a Will

It is sometimes necessary to change a will. A codicil is a legal document that amends a will. You might find it necessary to make changes when the following events occur:

- Marriage, remarriage, or divorce
- Birth of a child
- Move to another state
- Acquisition of additional assets
- Changes in federal and state laws

Divorce and separation can affect a will. In some states, divorce can revoke the entire will. In other states, it revokes only those provisions in the will that favor the former spouse.

For more information on wills, visit the FindLaw estate-planning page at http://www.public.findlaw.com/estate_planning/

5.f. Dying Without a Will

Dying without a valid will is called dying “intestate.” If you die without a will, the laws of your state will govern how your assets are distributed. Whether you are single or married, it will be the laws of your state that determine how your property is transferred. You may also pay more in taxes for large estates.

To find an example of Kentucky's property-distribution laws, go to http://www.ca.uky.edu/agc/pubs/fcs5/fcs5425/fcs5425.pdf and access the article "Estate Planning: Wills and Probate in Kentucky." See page 2 for diagrams of “Property distribution for a person with a surviving spouse who dies without a will in Kentucky” and “Property distribution for a person with no spouse who dies without a will in Kentucky.” To review your own state laws regarding property distribution, check with your state bar association.

6. The Probate Process

When someone dies owning property (real property as well as tangible and intangible personal property), the law provides a legal procedure for settling the estate. This procedure, commonly called "probate," involves:

- determining what property the person owned and its value
- determining what debts the person owed
- distributing or assigning title of the person’s property to its new rightful owners

Federal and state estate taxes are also determined, although these must be paid even if no probate procedure is required.

Not all property is subject to the probate process. Examples include:

- property held in a living trust (although similar steps are generally followed by the trustee—but without court supervision)
- property held in joint tenancy with rights of survivorship
- property with a named beneficiary (unless the estate is the beneficiary); for example, life insurance cash value, Individual Retirement Accounts, U.S. savings bonds

After notice is given, state law will allow a period of time—varying from state to state—for creditors to make claims against the estate for debts owed them by the decedent (the person who died). The estate must remain open at least as long as the time allowed for filing claims against it. In certain circumstances, with court approval, an estate may be administered as a "simplified estate" for which direct court supervision of the personal representative's activities is not generally required, except to open and close the estate.

In a few cases, no probate proceeding is required. An example is if the decedent had no outstanding debts (or if any debts are assumed and paid by other people) and had no interest in property subject to the probate process. Another example is if the value of the estate is under a specified monetary amount.

6.a. Steps in the Probate Process

Steps in the probate process include:

- Petition for probate of the will or administration of the estate
- Appointment of a personal representative
- Notice to creditors
- Assembly, inventory, and appraisal of property
- Classification and payment of demands against the estate (such as debts of the decedent and liens against his or her property)
- Determination of homestead rights and family allowances
- Management (and sale, if necessary) of property
- Payment of state and federal taxes
- Accounting to the court and distribution of property

7. Personal Representative: To Carry Out Your Wishes

The person who carries out the plan for settlement of an estate is called a "personal representative." This can be a family member or trusted friend, a bank with trust authority, or a trust company.

The court determines whether a proposed personal representative named in a will or trust is legally competent to serve. If legally competent, the court will appoint that person. If there is no will or trust naming a personal representative, a personal representative is named by the court.

Settlement of a decedent's estate involves continual contact with the court. Various legal rights and responsibilities must be determined. For that reason, the personal representative should hire an attorney for assistance. The choice of an attorney is made by the personal representative, although a person can state in his or her will or trust a preference for a particular attorney to help in administration of the estate. If the decedent's debts exceed the estate's assets, you should consult an attorney before taking any action with the estate.

7.a. Duties of and Selection Criteria for the Personal Representative

The personal representative:

- Proves the will in probate court
- Collects and inventories property
- Pays bills and collects debts
- Files tax returns
- Manages probate property

- Defends or brings lawsuits, if needed
- Distributes property

Choose your personal representative carefully. The person you select must be:

- Able to do the job
- Willing
- Able to keep peace among family members
- Able to meet legal requirements
- Conveniently located nearby, if possible

8. Gifting and Tax Strategies

It is important to evaluate the effects of federal and estate taxes on estate planning. An estate may be subject to taxes before it is distributed to beneficiaries.

A specified portion of an estate is exempt from estate taxes. During 2004 and 2005, the first $1.5 million of an estate could be distributed to children or others tax-free. The Tax Relief Act of 2001 increased the tax-exempt level to $2 million for the years 2006 to 2008 and $3.5 million for 2009. Federal taxes are imposed when your estate exceeds the limits mentioned.

Federal estate taxes on the taxable portion of the estate range from 45% to 48%. The Tax Relief Act gradually reduces the maximum tax rate to 45%.

While most gifts or estates are not large enough to pay federal tax, you should estimate your estate taxes based on your net worth. If your net worth is at or above the federal taxable limits, you can use strategies such as trusts, gifts, and contributions to minimize your tax liability. To assess your estate's value, add all assets, subtract any liabilities (including your mortgage), and also deduct funeral and administrative expenses. Do this periodically, as persons who have saved or invested for many years can have larger estates than they anticipated.

Keep in mind that if your estate's value exceeds the exemption, the assets subject to tax upon your death may include cash, life insurance policies you owned, stocks and bonds, the family home, the family farm, tangible personal property (such as jewelry, clothing, art, furniture, china, computers, power tools, etc.), benefits under employee benefit plans, and retirement assets such as Individual Retirement Accounts.

8.a. Gifts and Unlimited Marital Deduction

A gift is a tax-free distribution of funds from one person to another. The 2006 Internal Revenue Service code allows you to give cash and/or property valued up to $12,000 to each of an unlimited number of recipients per year without tax consequences. A married couple can give up to $24,000 per year, per recipient.

Gifts made to recipients over time can help reduce a large estate, and the gifts are tax-free to recipients. The unlimited marital deduction permits gifts of any size to your spouse during life or at death without tax consequences.

More details can be found in IRS Publication 950, "Introduction to Estate and Gift Taxes," at http://www.irs.gov/publications/p950/index.html.

A word of caution: gift and transfer rules for Medicaid are much more restrictive than tax rules. The rules for Medicaid—which pays for 70% of all nursing home care—vary widely from state to state. If a nursing home stay is likely in the next five years, consult an elder-law expert before making any significant gifts.

9. A Trust: Who Needs One?

Reasons for Having a Trust: A trust is a property arrangement whereby a trustee (such as a bank trust department or a person) takes care of, holds title to, and, in most cases, manages property for the benefit of someone else. Trusts are not for everyone but can fit the needs of certain people, including those whose estates approach or exceed the federal tax limit and those with young children or disabled family members who are unable to manage their own affairs. Various types of trusts are designed for different situations and circumstances.

It is important to understand terms related to trusts:

- *Grantor, settlor,* or *trustor* is the person who creates the trust
- *Trustee* is the person or entity named to carry out the instructions contained in the trust document; he/she also holds legal title to and manages the trust property
- *Beneficiary* is the person who benefits from the trust
- *Revocable* trusts allow you or someone you name to make changes in the document
- *Irrevocable* trusts cannot be made void, rescinded, cancelled, or reversed by anyone

Your personal circumstances will determine whether it is beneficial to establish a trust. Among the reasons commonly cited for setting up a trust are that it can:

- Provide payment for or reduce the amount of estate taxes
- Avoid probate and transfer your assets to your beneficiaries immediately
- Provide income for beneficiaries and a surviving spouse
- Free you from managing your assets while allowing you to receive a regular income from the trust
- Have your property serve a desired purpose after your death

A will is also needed to transfer any assets that have not been transferred before death and to nominate a personal guardian for children.

9.a. Types of Trusts: Testamentary and Living Trusts

Each of the various types of trusts available has particular advantages. An estate attorney can advise you about the type of trust that is most appropriate for you and your family situation. The testamentary trust and living trust will be discussed here.

A *testamentary trust* is a legal instrument contained in the will that sets up the management of assets for one or more beneficiaries following the death of the person creating the trust (grantor). This type of trust is created by the will and a trustee is named in the will. A testamentary trust is revocable until death or incapacity and has no effect until death and admission of the will to probate. This type of trust is generally used for minor beneficiaries or when you do not want beneficiaries to inherit the estate outright.

A *living trust* (also known as an intervivos trust) is a form of a contract entered into during the lifetime of the person creating the trust. It is established during the grantor's (creator's) life and may continue after the grantor's death. A living trust transfers property to heirs at the grantor's death without that property being subject to probate. A trustee manages the property and distributes the income and principal according to the grantor's instructions in the trust document. You will need a simple will to dispose of property that you did not put in the trust. You must remember to put property into the trust and to transfer title to the name of your trustee. A living trust should be accompanied by a pour-over will. This document will allow any assets that were not formally transferred to the trust during the life of the decedent to be "poured over" into the trust. These assets will then become part of the trust principal when the decedent dies. A living trust is a separate document and may have provisions that only take effect at the death of the grantor.

Living trusts can be revocable or irrevocable. With revocable trusts, you have control of the trust and can change the beneficiary, trustee, or other terms and can dissolve or revoke it. The person making the trust retains the right to use the property. The trust is used to manage assets and to avoid probate. Generally, assets still can be included in your gross estate for tax purposes.

Irrevocable trusts are permanent and cannot be revoked or changed. The grantor relinquishes all control over the disposition of the property placed in the trust and the income from it. This type of trust can have enormous tax advantages when the trust is not considered a part of your estate for tax purposes.

9.b. Advantages and Disadvantages of a Living Trust

Advantages:

- Avoids probate but not necessarily estate taxes
- Administers property in different states with one document
- Manages business and personal affairs during your life
- Manages assets if you become incapacitated
- Depending on state law, may protect separate assets in case of divorce
- Can pay medical and other bills and provide for scholarships
- Distributes assets faster to beneficiaries
- Provides privacy

Disadvantages:

- Expensive to draft
- Involves costs to update
- Expenses can outweigh benefits
- Not court-supervised
- To protect assets, the trust must be funded with them
- The need to update and fund the trust is ongoing

9.c. Is a Trust the Right Planning Device for You?

The decision to create a trust is a complex one. You will want to discuss your personal needs with financial and legal experts. It is not uncommon for an individual who owns a small parcel of land, a home, and a few investments to have an estate that exceeds the federal estate-tax limits, resulting in large tax implications. In addition, if you own assets that require ongoing management, such as rental property, a trust may help facilitate their management in the event of incapacity.

Individual situations and the purposes of your estate plan will determine the best strategies for you. However, unless you have an estate that exceeds the federal tax threshold, own complex assets, or are providing for a minor child or disabled person, under most circumstances you are not likely to need a living trust.

10. How to Hire and Work with an Attorney

If you want to draft a will, create a trust, or prepare a power of attorney, you will need to work with an attorney. An attorney is the only professional licensed to write legal documents. Look for one who specializes in estate planning or elder law. Complex estates such as those with investments, real estate, and/or business assets may require consultation with family members and financial management, tax, and legal experts.

Finding an Attorney

- Ask people you know if they can refer you to a good attorney. Friends, local business owners, or professionals such as accountants, financial planners, or bankers may be able to recommend attorneys who specialize in estate planning.
- Ask for referrals from lawyers. Most lawyers specialize in several areas of law. If a lawyer tells you he/she does not handle estate planning, ask him/her to refer you to someone who specializes in it.
- Look for duplicate referrals—that is, attorneys who are recommended to you by more than one source.

Another way to locate an attorney is to contact your state's bar association and request a lawyer referral. Bar associations do not rate attorneys, but they exclude from their lists lawyers who have had excessive complaints about them. You can find members of the American and state bar associations on the American Bar Association's Lawyer Locator Website, http://www.abanet.org/lawyerlocator/searchlawyer.html.

10.a. Attorney Ratings

Once you have the names of several lawyers, you can find additional information about them in the Martindale-Hubbell Law Directory, available in many libraries and on the Internet (see http://www.martindale.com/). The directory contains biographical information, experience, specialties, education, and other professional information. Some attorneys are not listed because they are new to the profession or practice in a rural location where there are too few other attorneys or judges to rate them.

Almost every attorney listed in the directory is rated AV, BV, or CV. The ratings are a compilation of confidential opinions that Martindale-Hubbell solicits from lawyers and judges. There are two components to each Martindale-Hubbell peer review rating. The first letter is for "Legal Ability," which is rated as follows:

- A—very high to preeminent
- B—high to very high
- C—fair to high

The second letter, V, stands for "Very High General Recommendation," meaning that the rated lawyer adheres to professional standards of conduct and ethics.

A Martindale-Hubbell rating should not be your only criterion for deciding on a potential lawyer. However, you can be reasonably confident that a lawyer who gets high marks from other clients and an AV rating from Martindale-Hubbell is knowledgeable and credible.

10.b. Interviewing Prospective Attorney Candidates

After narrowing the attorney list to two or three, contact the attorneys and request a face-to-face meeting. If you outline your needs in advance, many lawyers are willing to meet with you for a half-hour consultation at no charge. You should ask the attorney whether he or she charges a fee for an initial consultation. During this meeting, pay attention to your comfort level with the attorney. Ask all prospective lawyers:

- What is your experience in this area of law?

- How will I be able to contact you?
- To whom in your office can I talk if you are not available?
- How long will it take you to return my communication?
- Approximately how long will it take to complete my legal work?
- What are your rates and how often will you bill me?
- What can I do to reduce legal fees?

Many people are uncomfortable talking about fees, but these must be discussed early in an attorney-client relationship. Legal advice does not come cheaply. Lawyers commonly charge for their work on an hourly basis. Fees vary by region, by the complexity of the case, and by the experience of the lawyer. Rates may range from $60 to $300+ per hour. Attorneys may also offer a “flat rate” for certain types of work, such as drafting a will or trust. After selecting an attorney and before beginning legal work, get an agreement in writing.

One final question that is helpful is to ask is "What would you like to know about me?" More than any other, this question will tell you whether this legal adviser is a true pro. If he or she is not interested enough in you to probe now for full answers to critical questions, say good-bye. You may never get the treatment you deserve from a professional who shows little interest.

10.c. Deciding What to Include in Your Estate Plan

Once you have selected an attorney, decide what you want your estate plan to achieve before scheduling a second, longer meeting. Determine:

- Do you want to make sure that your spouse/partner is financially secure?
- What do you want to happen to the property you have accumulated?
- Who will care for your minor children or aging parents?
- Do you want your spouse and children to be provided for in an equitable manner?
- Who will settle your estate in a timely and fair way?
- If you own a business, do you want one or more family members to inherit and manage it?
- Do you want to keep estate taxes, probate fees, and other administrative and legal costs to a minimum?

Organize and prepare important lists and inventories. You will need many of these papers to complete your estate plan. See the lesson Organize Your Important Papers for forms that you will find useful.

10.d. Preparing a Checklist for Meeting with an Attorney

As you begin your estate plan and before you meet with attorneys and other financial advisers, it is helpful to assemble the following information. Having this information readily available will save you time and money in legal fees. It will also help you think through your wishes for distributing your estate. Use the Record of Important Papers, Household Inventory, and other forms in the Organize Your Important Papers lesson to assist you. Include in your list:

- Names, addresses, and birthdates of your spouse, children, and other loved ones whom you wish to include in your will; if applicable, list any disabilities or special needs
- Names, addresses, and phone numbers of possible executors, trustees, and guardians of young children
- Amounts and sources of income, including interest, dividends, and other household income
- Amounts and sources of debt, including business debt, mortgage(s), leases, and outstanding loans
- Amounts, sources, and beneficiaries of retirement benefits, such as pensions, Individual Retirement Accounts, Keogh accounts, government benefits, and profit-sharing plans
- Amounts, sources, account numbers, and other information related to financial assets, such as bank accounts, annuities, joint owners, and payable-on-death designees
- Life insurance policies, including issuer, owner, beneficiaries, account balances, and amounts borrowed against the policies

- Valuable property you own, its approximate value, and the names of the people to whom you wish to leave these items; include such property as real estate, furniture, jewelry, collections, and heirlooms
- Names of trustees, assets, and trusts held for your benefit
- Other documents that might affect your estate plan, such as divorce decrees, tax returns, pre-nuptial agreements, marriage certificates, wills, trusts, and property deeds

Case Studies and Resources

Initiating Discussions about Property Distributions

Do you have concerns about property-distribution issues? Discuss these particular situations with your adult children, trusted friends, or parent/guardian. The correct responses are provided for residents of Idaho, Iowa, Kentucky, North Dakota, and South Dakota.

- Prepare Your Estate Plan Case Study 3: The disadvantages of writing your own will
- Prepare Your Estate Plan Case Study 4: The surviving spouse's share
- Prepare Your Estate Plan Case Study 5: How much will each heir inherit?
- Prepare Your Estate Plan Case Study 6: The dangers of making someone a co-owner of a bank account as joint tenants with right of survivorship

Resources

- “Critical Conversations about Financing Long Term Care” (about long-term care concerns that could affect property inheritance): http://www.financinglongtermcare.umn.edu/pdfs/conversationstarters/criticalconversations.pdf
- “Talking with Aging Parents about Finances” (see “Family Finance Discussion Points”: http://www.montana.edu/wwwpb/pubs/mt9324.html
- About Health Care Advance Directives [Link to Communicate]
- “Who Gets Grandma's Yellow Pie Plate?" (provides methods and discussion for distributing untitled property): http://www.yellowpieplate.umn.edu/indexB.html
- "Estate Planning: Wills and Probate in Kentucky," Suzanne Badenhop, Ph.D., Extension Specialist, Family and Consumer Sciences (provides a Kentucky example of how property is distributed with or without a will). Download a copy at http://www.ca.uky.edu/agc/pubs/fcs5/fcs5425/fcs5425.pdf

Return to the Prepare Your Estate Plan learning lesson.

Browse related Articles by tag: personal finance, financial security: legal topics

This resource area was created by the: Personal Finance community

---