

::personal estate planning course lessonbook

So you can keep more of what's yours and give to those you love and support

Five lessons designed to help you understand the benefits of smart estate and gift planning

::learnhowto...

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:: lesson one

How You Can Shape the Future



What you'll learn

In this lesson, we'll discuss the steps you should follow in putting together an estate plan that meets your goals. We'll also warn you about dangerous misconceptions. You'll learn key facts about wills and trusts. You'll discover how estate planning can enable you to manage your investments more profitably and how qualified professionals can help you through the planning process.

What Is Estate Planning?

If you have possessions, you have an estate. Their orderly care during your lifetime represents financial management. Their disposition after your lifetime is called estate settlement. Deciding in advance how this will be done is known as estate planning. Estate planning is that simple.

You plan for the sake of the people in your life. Don't become so engrossed in the legal and tax complexities that you lose sight of the welfare and comfort of those you want to help. And while you are planning for the financial needs of others, your first concern should continue to be your own security and standard of living.

Who Needs It?

Perhaps you feel that estate planning is only for the very rich—the Forbes 400, certainly. Without a doubt, estate planning is for those who are wealthy. But is estate planning for everyone? For you?

One school of thought says the more modest your estate, the greater your need to arrange for its careful handling and disposition—to make it stretch further and to help those closest to you.

Look at the full extent of your assets. When the matter of resources comes up, there's an inclination to focus on stocks and bonds and money in the bank. But your

possessions may include other assets that have value, such as your home, life insurance, retirement accounts, and real estate or business investments.

On occasion, people think that some arrangement or law will solve their estate planning problems. For example, they mistakenly assume that joint ownership will take care of matters. Or they believe that state law will ensure that their estate will be left in the proper proportions to those whom they desire.

These are dangerous and shortsighted misconceptions that can be costly. Anyone who has possessions—property of any kind—needs a carefully organized estate plan. Obviously, the greater the value of your assets and the more diverse your wishes, the more important your need for a proactive plan to cut taxes and costs.

Setting Your Estate Planning Goals

Now let's talk about your objectives. We'll start with a basic assumption: You want to keep taxes and administration costs as low as possible. Beyond that, what's important to you?

Yourself. You might assume that estate planning has nothing to do with you personally, except to see that your property

Did You Know?

You should review your estate plan every couple of years and whenever you have major updates in your life, such as a change in marital status, the birth of a child or a relocation to another state.



Watch Out

There are no shortcuts in estate planning.

So beware of do-it-yourself approaches. A canned plan that seems suitable for your situation on the surface may actually be a poor choice after you dig into the details. Why risk leaving a costly mistake (financially, emotionally or both) to loved ones later to save a few bucks now?



is taken care of when you're gone. This outlook represents a common error.

Smart estate planning involves a generous measure of financial management during your lifetime. As you grow older and your assets increase, you may want to lighten your own responsibilities while ensuring that in the event of sickness or disability, your investments will be prudently managed and your financial obligations met. What's more, planning for the future needs of others can employ vehicles that offer you lifetime advantages, such as a living trust or a life income arrangement.

Your family. If you're married, you and your spouse should decide how your assets will be administered for the maximum advantage of the survivor. When you are gone, your spouse will face new and heavy burdens.

If you have children or grandchildren, what are their special needs? Give serious thought to their lack of experience or any mental or physical disability that may affect their competence to manage their own

finances and any assets you leave to them. Remember, you won't be around to make the decisions.

Are there other relatives who are dependent on you? Consider their requirements should they survive you.

What about any business enterprise in which you have an interest; what will happen to it? You may want one or more of your children or business associates to own and manage it after your death.

Your philanthropic interests. Don't overlook worthy causes that advance education, maintain excellence in health care, provide care for less fortunate individuals, and support religious and social service organizations in which you are interested. There's no better way to influence the future than through charitable gifts after your lifetime. Your concern and foresight can secure for you a unique kind of immortality.

Naturally you want your charitable goals to harmonize with the needs of your family. Their support and comfort come first. Surprisingly, careful planning can allow you to satisfy both family and charitable goals.

6tools Essential Estate Planning Documents

1. Your will

This document disposes of your property upon your death. A phrase such as "all the rest, residue and remainder of my estate" will ensure that any assets controlled by your will and not otherwise mentioned in your will pass to those you want to receive them.

2. A trust

This is an arrangement for the management of your assets. There are many kinds of trusts, but they all share this common definition: "A fiduciary relationship in which the trustee holds title to property (the trust principal) for the benefit of another (the beneficiary) during the trust term."

And the tax savings permitted by our nation’s laws encourage these mutual objectives.

Begin Your Action Plan

The first step in creating your estate plan is to prepare an inventory of personal data. After you complete this course, we will provide you with a practical record book to help you start this process.

Without the basic facts that you will detail in your record book, your estate plan can’t be fashioned intelligently.

The model estate inventory on Page 6 illustrates the financial picture of George and Martha using current market values. This straightforward approach makes it easy for you to ensure that you have covered all the essentials of your own estate inventory.

When you review your present plans and title arrangements, you may be astonished by what you learn. All too often, even the best estate plan becomes outdated by changing personal and financial circumstances, and new tax laws.

Recognize the Pitfalls

It is not our purpose to train you to become an estate planner—even for your own estate. To become accomplished in this legal and financial field requires years of experience. But we can alert you to errors that can cause great unhappiness for those you hold dear and deprive them of funds they may need to live comfortably. Moreover, your future well-being may depend on the plans you make now.

In estate planning, the worst mistake of all is procrastination. People know they should make plans, but for one reason or another they don’t get around to it. When the unexpected occurs, others are forced to pick up the pieces of a confusing financial puzzle.

There is a better way—a personalized estate plan.



3. Life insurance policies

These provide for payment of the face value to your designated beneficiary upon your death. This beneficiary may be an individual, a trustee or a charity. Or you can have the proceeds held by the insurance company for payment of either interest or fixed installments to your beneficiaries.

4. Deferred employee benefits

These include pension or profit-sharing benefits, a 401(k) or Keogh plan, an IRA, group life insurance and stock options. They have written provisions for their disposition upon your disability, retirement or death. Social Security can be another important benefit at such times.

5. Durable power of attorney for finances

This ensures that someone you trust will have legal authority to take care of financial matters if you cannot. (The term “durable” means that the document remains effective if you become incapacitated.) The tasks may range from paying bills to filing taxes.

6. Living will and health care power of attorney

These forms explain your health care wishes. A living will directs your doctor to withhold or withdraw life-prolonging interventions if you are terminally ill or permanently unconscious. A health care power of attorney allows you to name a person to make decisions for you.

quizone

Select the answer you believe is correct. You'll find the key below.

1. Estate planning is

- a. only for the rich.
- b. vital for anyone who has assets.
- c. required by law.

2. The first step of every estate plan is to

- a. prepare a personal inventory.
- b. draft a will.
- c. make a list of insurance policies.

3. Estate planning experts include

- a. actuaries.
- b. estate planning attorneys.
- c. IRS agents.

4. One tool of estate planning is a

- a. durable power of attorney.
- b. computer.
- c. mutual fund.

5. Trusts are useful in

- a. replacing wills.
- b. managing assets.
- c. ensuring nothing is overlooked.

6. Good estate planning involves

- a. completion of an estate tax return.
- b. owning sufficient assets.
- c. financial management during your lifetime.

7. Experts say that the more modest your estate

- a. the greater the expenses.
- b. the shorter the will.
- c. the greater the need for careful disposition.

Answers to Lesson One Quiz:
1. b; 2. a; 3. b; 4. a; 5. b; 6. c; 7. c

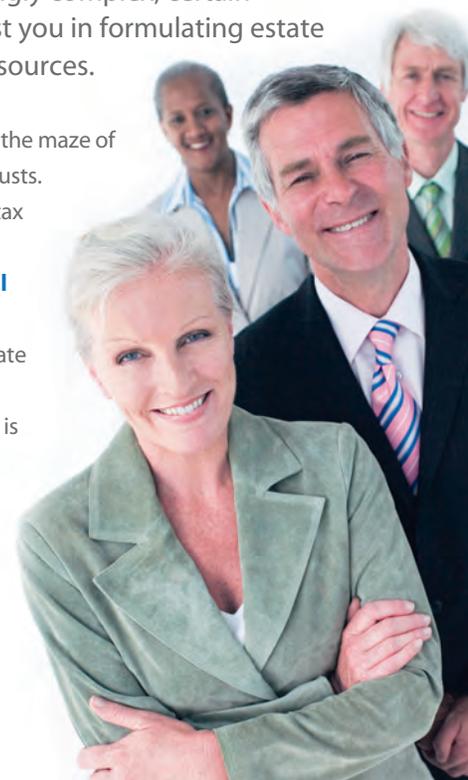
Model Estate Inventory

Assets	George	Martha	Joint
Residence			\$500,000
Bank and money market accounts	\$20,000	\$25,000	\$40,000
Mutual funds	\$15,000	\$10,000	
Listed securities	\$100,000	\$25,000	
Note receivable from son	\$10,000		
Business interest (51% of outstanding stock)	\$250,000		
Life insurance	\$250,000	\$50,000	
Furniture and automobiles			\$60,000
Oil paintings and jewelry			\$30,000
401(k) plan and IRAs (payable to each other)	\$500,000	\$125,000	
Total assets	\$1,145,000	\$235,000	\$630,000
Liabilities			
Mortgage on residence			\$100,000
Life insurance loans	\$15,000		
Other debts	\$15,000		
Total liabilities	\$30,000	\$0	\$100,000
Net worth			
Assets less liabilities	\$1,115,000	\$235,000	\$530,000

seektheexperts

As financial and tax matters become increasingly complex, certain professionals offer skills and expertise to assist you in formulating estate plans. Find qualified referrals from reputable sources.

- » An **estate planning lawyer** is needed to interpret the maze of laws on property rights, taxes, wills, probate and trusts.
- » A **certified public accountant** who specializes in tax matters can analyze the tax impact of estate plans.
- » A **financial advisor or life insurance professional** offers advice on ways life insurance can build your estate and provide the liquid funds needed for estate taxes or a business buyout agreement.
- » A **trust officer's** experience in administering trusts is valuable in discussions of personal and investment aspects of fiduciary relationships.
- » A **charitable gift planner** represents a charity and can explain the array of gift plans available to meet your needs, save taxes and serve the organization's goals.



:: lesson two

How to Make a Better Will



What you'll learn

In this lesson, we'll discuss why everyone needs a will, if probate is necessary and whether joint ownership can take the place of a will. We'll explain why a will has to be so long and why all that legal jargon is necessary.

What's a Will?

A will is a legal document that transfers some of the assets held in your individual name to your beneficiaries when you die. It also names the executor whom you want to carry out the terms of the will and a guardian for any minor children.

Making It Valid

To create a valid will, you must be of sound mind and legal age. Even if you're incompetent, you may at times have lucid moments when a valid will can be executed. A will made under threatening circumstances ("Sign this or else!"), however, can be invalidated.

Mighty court battles have been fought over the validity of a will, so the signing ritual is important. The procedure varies, but it may begin with your attorney asking, "Do you declare this to be your last will and testament?" and "Do you request these people to witness your signature?" Most states require at least two witnesses to the testator's signature, and both witnesses must be present when the testator responds to the above questions and signs the will. The witnesses, however, do not need to know the contents of the will.

Many states allow the addition of a self-proving affidavit to a will. This document is notarized at the time of signing. Ultimately,

the affidavit can be offered to the court for proof that the will was signed properly. If no one objects, the affidavit will avoid the necessity of bringing one or more of the witnesses before the court after the testator's death to testify as to the signing.

Generally, a will that was validly made in the state of a person's domicile will need to be redone if that person moves to another state because each state has its own requirements for a valid will. A newly revised will establishes your new legal residence, provides local witnesses, establishes your executor's qualifications to serve in the new state and includes provisions facilitating settlement under the laws of the new state.

Your Invisible Estate Plan

People often think that a will controls the distribution of their entire estate. They forget that some assets are not included under its terms.

Three common methods exist by which some of your assets are transferred to your heirs after your death:

- » Beneficiary designation
- » Joint ownership with rights of survivorship
- » Will or trust

Did You Know?

About half of adult Americans die without a will. So what? That means the laws of your state determine what happens to your children and your assets. Not you!



Good to Know

Be careful to store important papers where they are safe as well as reasonably accessible; don't put your will in a bank's safe-deposit box, as it may be hard to access immediately after your death.



Beneficiary designations are common with life insurance, pensions, IRAs and 401(k) plans. When you name a beneficiary on these accounts, upon your death the accounts are distributed directly to your beneficiary without going through probate. Your will does not determine who will receive these benefits.

Jointly owned property with rights of survivorship generally goes to the surviving joint owner, regardless of what the will states. The same is true of one-half of community property in nine states.

If you own property jointly as tenants-in-common with another person, your one-half of the property will follow the provisions in your will; therefore, your beneficiary will become the new co-owner at your death with your original tenant-in-common.

It is important in the estate planning process to know how your assets will pass to your heirs and how they are owned—jointly or not, and if jointly, which type of joint ownership so that all your assets transfer to the proper beneficiary.

If you overlook these arrangements, you may hinder your overall plans. Ultimately, your oversight could result in additional taxes and administrative costs. For example, joint assets won't be added to a trust in a will that is designed to save estate taxes and provide professional investment management.

Inequity can occur unintentionally. For example, a widow wanted to treat her son and daughter equally, so she bequeathed each child one-half of her estate. But her sizable bank accounts were in joint names with her son so that he could pay her bills (a power of attorney would have sufficed). After she died, he received half of the estate controlled by her will (her "probate" estate) and also all the funds in the bank accounts. Imagine how her daughter felt!

Choose Your Executor

Once they've decided on the division of their assets, most people don't give sufficient thought to the choice of their executor (also known as the personal representative).

This is a crucial decision that you should start thinking about early in the

:::executor duties

- » **Petitions** the court to open probate and to admit the will
- » **Notifies** all beneficiaries included in the will, or intestate heirs, of the administration of the will
- » **Notifies** all creditors that probate is in process
- » **Collects** the deceased's assets and lists them in an inventory
- » **Seeks** court approval to sell any assets that might be necessary to pay debts
- » **Determines** and pays claims against the estate
- » **Pays** federal and state income and estate taxes
- » **Distributes** the estate's net assets, according to the court's order, to the will's beneficiaries, or heirs if there is no will
- » **Closes** the estate



planning stage. From the standpoint of your beneficiaries, on-the-job training of an executor can be a costly and unhappy experience.

Weigh carefully the nature of the many duties that must be assumed. Will your executor be able to carry them out properly? What is your proposed executor's knowledge of estate settlement, finance and investments, taxes, and record keeping? What about the availability and state of health of the individual? Will your choice of executor be impartial when dealing with your beneficiaries?

If you plan to name a bank or trust institution to serve as executor, visit that organization and talk with their officers before you make your decision.

If you have minor children, you should name a guardian of each child and each child's property (a custodian) in case your spouse doesn't qualify or doesn't survive you. Otherwise, the court may appoint someone you might not have chosen.

Don't Expose Your Estate to Chance

You need a current will whether you are single or married, young or old, and whether your estate is modest or large.

Any updates to your will should be made by your attorney to ensure that changes are valid. Your will may seem overly long, but your attorney needs to write in a specific style. This is necessary to express your wishes for the disposition of your property under all circumstances while giving your executor the powers needed to do the job properly.

Instead of dreading the event, consider your will-making appointment with your attorney as an opportunity to plan how you can benefit your family, friends and charities in a creative manner after your lifetime.



probate

What Is It?

Used in its original meaning, probate refers to the court process for determining the validity of a deceased person's will. By custom, the entire process of settling an estate has become known as probate. Here's the actual process:

1. **Collecting** and safeguarding of assets
2. **Paying** proper claims
3. **Filing** tax returns
4. **Managing** investments and other property
5. **Distributing** estate assets according to the terms of the will

The process of probate is intended to protect and direct the distribution of property according to your will. But not all of your assets go through probate. Most life insurance and retirement plans, assets you own jointly with rights of survivorship, and assets owned by a revocable living trust do not pass according to the terms of your will and avoid the probate process.

Living trusts are a popular option for passing on assets. In general, the greater the value of your assets, the greater the potential value in having a living trust. Most revocable trust-based estate plans, however, have companion wills that require a limited form of probate. For more on living trusts, see Page 12 of this booklet.

8 Ways to Establish Bequests

The gifts in your will can take various forms. They can be cash or personal and real property. They can be shares of the residue of your estate. They can be given outright or in trust. You can designate your gift for a specific purpose. A charitable gift can be unrestricted, restricted or contingent.

Here are eight generally accepted ways to make a bequest. Discuss them with your attorney as you prepare to plan or update your will.

Question



Do you really need a lawyer to draft a will?

Yes. Only attorneys licensed to practice law are qualified to draft wills; do-it-yourself kits can spell disaster.

1 Specific bequest. This is a gift of a specific item to a specific beneficiary. For example, “I give my golf clubs to my nephew John.” If you no longer own the golf clubs at your death, the bequest fails and John cannot claim any other property. (In other words, John wouldn’t receive cash for the value of the golf clubs instead.)

2 General bequest. This is usually a gift of a stated sum of money. It will not fail, even if there is not enough cash in your estate to pay this bequest. For example, “I give \$50,000 to my daughter, Mary.” If there is only \$2,500 cash in the estate, other assets must be sold to pay the bequest.

3 Contingent bequest. This is a bequest made on condition that a certain event must occur before distribution to the beneficiary. For example, “I give \$50,000 to my son, Joe, provided he enrolls in college before age 21.” A contingent bequest is specific in

nature and fails if the condition is not met. (A contingent bequest is also appropriate if you want to name a secondary beneficiary, in case the primary beneficiary doesn’t survive you. For example, “I give my stamp collection to my friend Susan, provided she survives me. Otherwise, I give my stamp collection to my friend Patty.”)

4 Residuary bequest. This is a gift of all the “rest, residue and remainder” of your estate after all other debts, taxes and bequests have been paid. For example, let’s say you own property worth \$500,000 and you intend to give a child \$50,000 by specific bequest and leave \$450,000 to your spouse through a residuary bequest. If the debts, taxes and expenses are \$100,000, there would only be \$350,000 left for the surviving spouse.

Therefore, most attorneys agree that the preferred method to ensure that your beneficiaries receive the proportions you desire is to divide your estate according to percentages of the residue (rather than specifying dollar amounts).

quiztwo

Select the answer you believe is correct. You'll find the key below.

The previous four methods can apply to bequests for individuals or charitable organizations. The following four items are special considerations when you plan a charitable bequest.

5 Unrestricted bequest. This is a gift for the charitable organization's general purposes to be used at the discretion of its governing board.

A gift like this—without conditions attached—is frequently the most useful because it allows the charity to determine the wisest and most pressing need for the funds at the time of receipt.

Here is sample language that your attorney could include in your will when making this type of bequest: "I give and bequeath to [legal name and address of charitable organization] [dollar amount, percentage of residuary estate or description of property] to be used as determined by its governing board."

6 Restricted bequest. This type of gift allows you to specify how the funds are to be used. Perhaps you have a special purpose or project in mind. If so, it's best to consult with the charitable organization when you make your will to be certain your intent can be carried out according to your wishes.

7 Honorary or memorial bequest. This is a gift given "in honor of" or "in memory of" someone. Charitable organizations normally have many ways to grant appropriate recognition.

8 Endowed bequest. This bequest allows you to restrict the principal of your gift, requiring the charity to hold the funds permanently and use only the annual investment income or a small percentage of the total fund each year. Creating an endowment in this manner means that your gift can continue giving indefinitely, and you can leave a lasting legacy.



Watch Out! 

Be very careful to accurately name your beneficiaries. No one receives anything from your will unless complete and accurate names are used.

- 1. A self-proving affidavit**
 - a. simplifies proof of the witnesses' signatures.
 - b. lets a testator witness his or her own will.
 - c. establishes a testator's competence.
- 2. If you have minor children, your will should name a**
 - a. testator.
 - b. guardian.
 - c. probate attorney.
- 3. Witnesses to a will must be present**
 - a. when the testator decides on its terms.
 - b. when it is executed.
 - c. only when requested by an attorney.
- 4. When a person moves to another state,**
 - a. his or her will is invalidated.
 - b. a new will must be executed.
 - c. a revised will is advisable.
- 5. If a person dies without a will,**
 - a. probate is simplified.
 - b. all assets become state property.
 - c. state law determines how the estate will be divided.
- 6. Jointly owned property with rights of survivorship generally**
 - a. passes by will.
 - b. passes to the surviving joint owner.
 - c. passes to the named beneficiary.

:: lesson three

How Trusts Can Improve Your Estate Plan



What you'll learn

In this lesson, we'll look to trusts as new ways to protect your family and your money. We'll explain how the right trust can help you cut taxes and probate costs, and broaden your estate plan.

What's a Trust?

Simply stated, a trust is an agreement by which a person appoints someone to carry out specific or generalized services of financial management.

Those establishing a trust and providing the initial assets are called **grantors**. The **trustee**, appointed by the grantor, is responsible for providing the managerial services required by the trust agreement. **Beneficiaries** are those who receive income and/or principal from the trust and the **remaindermen** are those who will receive assets at the end of the trust. You can set up a trust for anyone for almost any purpose. Here are some typical trust arrangements:

Bypass trust. You can create a trust in your will—known as a **testamentary** trust—for the benefit of your spouse, children or others you select.

With this type of trust, you direct the trustee to pay the income to or for the benefit of the people you name. In addition, you can authorize the trustee to advance principal for the needs of your beneficiaries (an arrangement sometimes called “invading” the principal).

In a typical bypass or family trust, one spouse sets up a trust in his or her will for the other spouse's benefit and directs that after the other spouse's death, the trust shall continue for the support of their children until the children attain a certain age, say 25 or 30. Then the trustee is to turn over the principal to the children.

Living trust. You might decide to create a trust for your own benefit—a trust that will remain operative while you are living. It is logically called a living or **inter vivos** (Latin for “between living persons”) trust. In this case, you direct the trustee (you can name yourself trustee) to look after the trust assets, pay you the income and counsel you about the investments. You can be kept fully informed about all transactions and can reserve the right to amend or revoke the trust, add or withdraw assets, and, in some cases, approve investment changes. The trust can continue after your lifetime for the benefit of your family or others, and the trust assets avoid the costs and delays of probate.

Charitable remainder trust. You can set up a trust to pay income to yourself or someone else you choose for life

Did You Know?

A majority of states allow you to create a trust for your pet's care during its life, with the remainder left to whomever you designate. Consult your attorney to see if a pet trust is appropriate.



with the remainder going to a favorite charitable organization. The organization won't receive any benefits until after your lifetime (or after the lifetime of your spouse or other income beneficiary named by you.)

These charitable trusts can be measured by lifetime, by a set term of years (not to exceed 20) or certain combinations of the two. The trustee can be any person or bank or trust company, with successor trustees or co-trustees named, if appropriate.

A type of "life income" gift, this plan offers you many benefits: sizable income tax savings; potentially more income; a way to diversify investments while, for most donors, paying no up-front tax on their appreciation; and income for a survivor if desired. It's also possible you and your family may receive more than you originally gave. Such results depend on many factors, including the size of your estate, the income tax savings (for a trust funded during your lifetime), the investment yield on those savings, the payments received from the trust and the potential estate tax savings.

What Goes Into a Trust?

You can put most types of assets into a trust, providing the trustee is willing to receive it.

Suppose you fund a trust with cash. It is then the trustee's job to put the money to work in prudent investments.

Frequently, the grantor puts existing investments into the trust, expecting the trustee to hold them and make changes only when warranted. Types of investments used to fund trusts include stocks, bonds and money market securities. Real estate and other types of assets are also held.

The size of a trust depends on its purpose. A trust can hold virtually all your assets or only that portion you want held for a certain beneficiary. There is no minimum size for a trust except what is practical. Corporate trustees—banks and trust institutions—usually have a minimum fee; therefore, administration of very small trusts by a corporate trustee is normally uneconomical.

Question

Who does not need a trust?

It depends on the type of assets you own, the size of your estate and your plans for it. If you have few assets now—you're young and single, or newly married and just starting out—you can skip a trust for a while.



:: trusts irrevocable/revocable

You can't make changes.

You lose control over the assets.

Once assets are transferred in, you cannot remove them.

You may be able to reduce federal estate taxes.

You can modify them until you die.

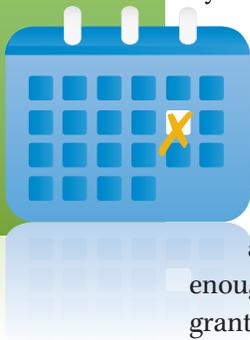
You control assets and pay the taxes.

You can transfer assets in and out easily with no annual limits.

They may be taxed as part of your federal estate.

Good to Know

Keep in mind a trust might not exist forever. It can last up to a date you specify in the trust document or until a particular event occurs—the date a child reaches a particular age, for instance, or when the amount in the trust is too small to administer. Many states limit a noncharitable trust to a specified term of years.



How a Trust Gives Protection

If you create a trust, you may be motivated by a desire to protect the trust beneficiary, preserve the trust assets or both.

If you make yourself the initial income beneficiary of a living trust, more than likely you do so because you want to provide for future needs. For example, if you are busy, travel a lot or become incapacitated, you would like the trustee to act in your best interest on investment matters and perhaps even to pay your bills. After your lifetime, you may want to have the trust income or principal flow directly to family and avoid the costs, delays and publicity of probate.

If you prefer, you can arrange to have your trust become operative only after your lifetime and for any number of purposes. For example, a husband may want to be certain that his wife will have her financial needs met when he's gone. A parent may want to set aside funds in trust for children to see to their support and education until they are mature enough to manage for themselves. The grantor of a trust may want to be sure

that the beneficiary doesn't waste the assets and isn't subject to the self-seeking influence of others.

Making a Revocable Gift in Trust During Your Lifetime

If you are interested in making a charitable gift but want to keep control of your assets as long as you live, there are other methods besides the terms of your will. As in the case of a benevolent will, however, Uncle Sam won't let you deduct these revocable gifts for income tax purposes because you hold the ability to revise your plans. Still, these methods are worth considering when you want to show your commitment to an important cause.

You can create a revocable trust in which you place cash, securities and other assets. You will receive the income for life; if that is insufficient for your needs and wants, you can withdraw assets anytime. You specify, however, that a percentage of what is left in the trust after your lifetime will go to the charities you designate—with the balance going to your loved ones. In the meantime, you can do anything you want with the trust: add to it, amend it or even revoke it.

:: let your imagination roam

If you feel there's more to be said about trusts, you're right. We've only covered the basics. The elasticity of the trust concept offers innumerable possibilities. You may find it to be one of the most useful strategies in your personal estate plan.



acloserlook

Charitable Remainder Trusts

» A charitable remainder trust established by your will doesn't give you a charitable deduction on your income tax return because you have the right to change your will at any time. But there may be significant federal estate tax savings for qualified charitable remainder trusts, whether funded by the terms of your will or by a trust agreement during your lifetime. Moreover, if the assets of a lifetime charitable trust are payable to a charitable organization at your death and you are the income beneficiary—all the assets in the trust are usually exempt from estate tax.

» When you designate a survivor to receive income for life from a charitable remainder trust, part of the market value of the trust avoids any federal estate tax in your estate. The value deemed to be the organization's ultimate share is the part free from estate tax.

» The value of your survivor's right to life payments (computed at your death) is subject to tax in your estate with one important exception: that value qualifies for the marital deduction if your spouse is the only surviving noncharitable beneficiary. And so, by naming yourself and your spouse as the sole income beneficiaries, the full value of the charitable remainder trust is free from federal estate taxes.

who's the best trustee?

The best-planned trust will fail to achieve your goals if the trustee doesn't carry out the trust terms and duties properly. The task often involves long-term management because a trust may span several generations. It's wise to choose a trustee carefully. Here are some important attributes to seek:

- » Knowledgeable about investments and taxes
- » Sympathetic concern
- » Record-keeping ability
- » Reliable

As you can see, the qualifications of a good trustee are formidable. Some, but not many, individuals meet the test. Even fewer would take the job if they knew what was expected of them. For these reasons, a corporate trustee—a bank or trust institution with officers specially trained in trust management—is often a good choice.



quizthree

Select the answer you believe is correct. You'll find the key below.

1. **A living trust is another term for**
 - a. an inter vivos trust.
 - b. a testamentary trust.
 - c. a charitable trust.
2. **A trust can be funded with**
 - a. cash.
 - b. securities.
 - c. almost any asset.
3. **Trust terms should be as**
 - a. restrictive as possible.
 - b. broad as possible.
 - c. appropriate to the circumstances as possible.
4. **When you create a charitable remainder trust, your family can be**
 - a. income beneficiaries.
 - b. remainder beneficiaries.
 - c. either of the above.
5. **A trustee's most important duty is**
 - a. keeping good records.
 - b. managing investments prudently.
 - c. invading the trust principal.
6. **A charitable remainder trust in your will can save**
 - a. income taxes.
 - b. estate taxes.
 - c. income and estate taxes.
7. **The minimum size of a trust is determined by its**
 - a. grantor, depending on its purpose.
 - b. trustee.
 - c. beneficiary.

:: lessonfour

How to Handle Federal Tax Laws



What you'll learn

In this lesson, we'll discuss estate and gift taxes, and explain ways to lower your gross estate for federal tax purposes using the marital deduction, charitable giving and other tax-saving opportunities.

Did You Know?

When it comes to federal taxes and your estate's value, more is definitely not better! Sure, you may feel satisfaction when you figure out the actual size of your estate, but when you realize that estate taxes can take a big bite out of your estate, you may think differently.



What's an Estate Tax?

The subject of taxes has long provoked strong emotions. In fact, more than 200 years ago Benjamin Franklin introduced the now familiar maxim that nothing is certain except for death and taxes.

The convergence of these two inescapable events has resulted in the federal estate tax, which is simply the taxation of property held by an individual at the time of his or her death. Throughout history, federal estate tax has been implemented three times and, after providing revenue on a short-term basis, repealed. The latest introduction of the tax occurred during World War I and has been in effect in one form or another since, except in 2010 when it was repealed for one year.

Your estate may be subject to estate taxes if it is worth more than the basic exemption level, which changes often. To calculate the value of your estate, add up all the assets you own or that you have an interest in, including your home, life insurance face amounts, retirement plans, etc. Note that your "estate" for federal estate tax reasons is a different amount than your "probate estate."

What's a Gift Tax?

Gift tax is applied when you transfer property to another person while

receiving nothing or less than full value in return. The tax applies whether you intend the transfer to be a gift or not.

It is considered a gift if you give property (including money), the use of property or income from property without expecting to receive something of at least equal value in return. If you sell something at less than its full value or if you make an interest-free or reduced-interest loan, you may be making a gift.

The person making the gift is generally responsible for paying the gift tax. Under special arrangements, the person receiving the gift may agree to pay the tax instead. If you are considering an arrangement like this, please visit with your tax professional.

The general rule is that any gift is a taxable gift. There are exceptions, however, to this rule. For example, the following gifts are generally not taxable:

1. Gifts that are under the annual exclusion for the calendar year
2. Tuition or medical expenses you pay directly to a medical or educational institution for someone
3. Gifts to your spouse
4. Gifts to a political organization for its use
5. Gifts to qualifying charities

An annual *gift tax exclusion* allows you to make tax-free gifts to individuals



cost basis

What Is It and How Does It Affect You?

Cost basis is the original value of an asset (usually the purchase price), adjusted for such factors as stock splits, dividends and capital improvements.

As you consider making gifts, keep in mind that very different rules determine the cost basis of property for someone receiving a gift during your lifetime versus by inheritance after you're gone.

If your child receives property as a gift from you during your lifetime, his or her cost basis would be whatever your cost basis is. This is called carryover basis. That means he or she would owe tax on any appreciation during your lifetime, just like you would if you were to sell the asset yourself.

If your child inherits the property after your lifetime, his or her cost basis would be the fair market value of the property on the date you die. This is called "step-up in basis." That means all appreciation during your lifetime would become tax-free. This rule saves heirs billions of dollars every year.

» EXAMPLE

Your father owns stock with a cost basis of \$100,000. Today, the fair market value has increased to \$300,000. If your father gives you the stock as a gift today, your cost basis would be \$100,000. Instead, if your father passes away and you inherit the stock at your father's death, the cost basis would be \$300,000—its fair market value on the date of his death.

What difference does this make? If you sell the stock that you receive during your father's lifetime for \$325,000 shortly after you receive it, you would owe tax on a gain of \$225,000 (\$325,000 – \$100,000). If you sell it for \$325,000 shortly after you inherit it, you'd owe tax on a gain of only \$25,000 (\$325,000 – \$300,000).

Estate planning and tax laws are complex. You should always consult with a qualified professional to assist you in such matters.

during your lifetime up to a certain amount each year. For example, a grandparent could give the maximum amount to each of his or her children and grandchildren every year. If you expect to have an estate subject to substantial taxes, this strategy would reduce your eventual tax bill.

If a married couple wants to make a gift, they can give *double* what the gift tax exclusion is—even if only one spouse's assets are used (assuming the other spouse consents and a gift tax return is filed). This is known as gift splitting.

If your gifts exceed the annual exclusion amount, you can apply them to your lifetime exemption, which allows you to make up to a certain amount in gifts during your lifetime without paying any out-of-pocket gift tax. Once that exemption is used, gift taxes apply.

Factoring in Generation-Skipping Transfer Taxes

This tax is less frequently seen and applies in addition to the estate tax. If you leave more than the exemption level in property to a grandchild or anyone two or more generations younger than you, your estate will incur taxes on the inherited property.

Double Your Tax Benefits With Gifts to Charity

We already mentioned that there is no gift tax on gifts to qualified charitable organizations. In fact, a gift may entitle you to a charitable deduction against your income tax if you itemize on your tax return. Turn the page to uncover some other ways to minimize taxes and shelter your estate dollars.

Good to Know

There is a deadline for paying the estate tax.

Usually it's nine months from the date of death. There are special installment payment provisions, however, for certain family farms and small corporations.



3 Ways to Shelter Your Estate Dollars

If you think your estate is subject to federal estate tax, consult with an estate planning attorney. Your attorney will discuss the current estate tax implications and create an estate plan that is designed to minimize federal estate taxes.

Your estate planning attorney may recommend the following estate planning techniques to reduce the size of your estate for federal estate tax purposes:

1

The marital deduction.

Generally, gifts and bequests to spouses are free of gift and estate taxes because of an unlimited marital estate and gift tax deduction (though special rules apply if the spouse is not a U.S. citizen).

Assets you leave in a marital trust (or a traditional estate trust under a will or trust agreement) will qualify

for the marital deduction, provided your spouse has the right to the income at least annually. In addition, your spouse must have the right to withdraw the principal during life or to direct its disposition at death to anyone he or she chooses.

Another plan to consider is a QTIP (qualified terminable interest property) trust. This trust qualifies for the marital deduction without giving away ultimate control of the trust assets. A QTIP trust pays your surviving spouse income for life. Then after your spouse's lifetime, the trust assets are distributed to the beneficiaries you named in your will or trust agreement.

2

The charitable deduction.

The government encourages gifts to qualified charitable organizations, so a bequest's value is completely exempt from federal estate taxes. There is no limit

FREQUENT BUT UNKNOWN

Taxes on Retirement Plan Assets

Some special planning is necessary if you want to pass the remainder of your retirement plan to heirs, whether it is an individual retirement account (IRA), a 401(k) or a tax-sheltered annuity. Whoever inherits the retirement plan money will have to pay income tax on it and, in some cases, estate taxes may also be assessed.

If you're planning a major charitable bequest, there's a planning opportunity that can result in the least impact on your family's inheritance: Designate a charity as the beneficiary of a percentage (1–100) of your retirement plan or IRA. Thanks to their tax-exempt status, charitable organizations receive 100 cents on the dollar.

Another option: Have your retirement plan flow into a charitable remainder trust after your lifetime. This trust can then pay your surviving spouse income for life.

Thereafter, the remaining balance in the trust can help fulfill our mission.

FACT

Who you name as the beneficiary of your retirement plan assets can have a big impact on how quickly the assets must be distributed to them after your lifetime, and thus, how quickly they are taxed.

Naming a spouse as primary beneficiary usually provides the most flexibility. For example, only a surviving spouse can roll over an inherited IRA distribution to his



quizfour

Select the answer you believe is correct. You'll find the key below.

1. Your estate is subject to estate taxes if

- a. you own any property.
- b. you die during a certain year.
- c. your estate's worth exceeds the federal basic exclusion amount.

2. An irrevocable life insurance trust is a way of

- a. eliminating gift tax.
- b. minimizing estate tax.
- c. selling life insurance.

3. The marital deduction permits unlimited tax-free gifts

- a. between spouses.
- b. by a married couple to their children.
- c. of personal effects.

4. Charitable bequests are free of estate tax

- a. up to 50 percent of adjusted gross income.
- b. when made to a QTIP trust.
- c. without any limit.

5. A beneficiary not subject to income taxes on a distribution from most retirement plan assets is a

- a. charitable organization.
- b. spouse.
- c. child.

6. Gift splitting is used by married couples to

- a. double the annual exclusion.
- b. divide funds among children.
- c. evade gift tax.

on the amount of the estate's deduction. This is different from the income tax charitable deduction for lifetime gifts, which is limited to an overall maximum for cash gifts of 50 percent of your adjusted gross income in any year.

A qualified charitable organization is any religious, charitable, scientific, educational or other entity described in section 501(c)(3) of the Internal Revenue Code. These may be public, private or governmental units. A trust or foundation operated exclusively for charitable purposes may qualify. Contributions to individuals generally are not deductible. Also deducted from your estate are any debts and mortgages you owe, plus the cost of your funeral.



Remove life insurance proceeds from your estate. Life insurance

is often a large portion of a person's estate. An irrevocable life insurance trust (ILIT) is an irrevocable trust that allows for the possible exclusion of life insurance proceeds from the estate tax. It is the most effective means of assuring that the proceeds of a life insurance policy are not included in your taxable estate.

Another way to reduce the size of your estate through life insurance is to name a charitable organization as the primary beneficiary of an existing or new life insurance policy. This will result in a federal estate tax deduction for the full amount of the proceeds payable to the charity.

or her own Spousal IRA and defer distributions until he or she then reaches age 70½.

Naming children and other individual beneficiaries of appropriately segregated accounts can allow those beneficiaries to stretch out the receipt of their benefits over their life expectancies—called a Stretch IRA—but note that distributions must begin the year after death.

(Naming a beneficiary other than your spouse may require the spouse's written consent.)

Deferring a portion of the distributions will eliminate immediate income taxation on the portion still deferred, but once distributed it will be subject to income tax at the beneficiary's tax bracket. A non-spouse beneficiary cannot defer the estate tax bill.

:: lessonfive

How to Cut Taxes Today by Changing the World Tomorrow



What you'll learn

In this lesson, we'll look deeper into trusts that serve special purposes, such as charitable lead trusts. We'll explain the benefits behind tax-deductible charitable gift annuities and deferred payment gift annuities, and we'll also tell you about a gift that gives you a tax deduction now for your home and allows you to live there your entire life.

Did You Know?

Your charitable deduction is available only for the net value of property you transfer to a charity. If you retain some interest in the property or give it to another noncharity, such as one of your relatives, the amount of the deduction will be reduced by the value retained.



Know the Gifts That Give Back

Many people underestimate the extent of their wealth. Without an inventory of your assets and personal property, you may not realize how much you have to give away. Your children may no longer need as much financial help as you are capable of giving. Perhaps there are charitable causes you would like to support in order to leave a legacy and perpetuate your values.

You could, of course, include a bequest in your will. There are other ways, however, to make contributions that promise lifetime benefits.

You can actually increase your income and reduce your taxes by making a life income gift. The recipient of your benevolence can't use your contribution now, but after your lifetime they will receive a welcome sum for their important work. One kind of life income gift is a charitable remainder trust (*discussed in more detail on Page 15*). With this gift, the organization's use of the money or property is deferred and will consist only of what remains after your lifetime.

In addition to an increased income and reduced income taxes, you receive other

valuable benefits from a life income gift, including the following:

- » Income, if desired, for a surviving spouse or other beneficiary
- » A way to diversify appreciated assets
- » Elimination of up-front capital gains taxes
- » Reduced investment worries
- » Potential estate tax savings

6 Ways to Donate

1

Annuity Trust or Unitrust

When you create a charitable remainder trust, you can choose from two types: an annuity trust or a unitrust.

Example: John gives securities to a trustee of a charitable remainder trust he creates. His trustee agrees to pay him an income for as long as he lives. These payments are either a fixed amount of money (annuity trust) or a variable amount based on a fixed percentage of the annually determined value of the assets (unitrust), whichever he chooses at the outset. On his death, the remaining balance in the trust is payable to the organization he has chosen.

You can fund the trust with cash or almost any other asset you wish, subject to the

trustee’s willingness to accept it. Moreover, you can increase your income by funding the trust with appreciated property that yields a low return. You do this by arranging for a payout that assures you a higher level of return.

If you sold the property, you would generally pay a significant percentage of federal tax on the capital gain. But the gift to a charitable remainder trust escapes this up-front tax.

How These Trusts Work for You

You determine how you want your charitable remainder trust to work.

First, you decide how much to put into the trust. Next, you consider how much income you would like to begin receiving from the assets. Finally, you decide whether you want a fixed or variable amount each year.

Which is better? Again, it’s up to you. If you want to receive a predictable dollar amount regardless of any fluctuation in the trust investments, then choose an annuity trust. But if you think the value of the trust assets is more likely to increase than decrease over the years, a unitrust is for you.

Naturally you would like the dollar or percentage figure for your trust to be as high as possible. This value is negotiable within limits as set by the IRS. But keep in mind that under IRS rules, your income tax charitable deduction is higher if you opt for a lower payout, an arrangement that lets you enjoy a larger tax savings at the outset.

Substantial Advantages

An annuity trust and a unitrust both allow you an immediate charitable income tax deduction.

Assuming you itemize your deductions, in the year you establish your trust, you can take a sizable federal income tax deduction and carry over any excess and unused amount for up to five additional years. The deduction represents the present worth of the philanthropic organization’s remainder interest as determined by U.S. Treasury tables. The deduction is less when two people (perhaps husband and wife) are beneficiaries of the same trust, since payments are likely to continue longer.

2 Supplemental Retirement Plan

You can set up your retirement unitrust to supplement your qualified retirement plans. Unlike a company profit-sharing or pension plan, it’s a plan designed just for you. For higher income earners in their 40s or 50s, establishing a unitrust with multiple-year funding can be highly beneficial.

Example: George, 55, decides to contribute \$10,000 a year for the next 10 years to a unitrust to be invested primarily for growth. Because a charitable remainder trust is tax-exempt, the trustee can invest and reinvest without concern for capital gains taxes. At his retirement, George receives variable payments each year equal to a selected percentage of the market value of the trust assets as revalued annually.

You choose the fixed percentage at the outset. A unitrust can be a hedge against inflation because the annual amount you receive reflects any change in the value of the unitrust assets. You can also provide life payments for a survivor—such as your spouse.

Be Informed



There’s a way to learn as much as possible about your favorite charity—its history, programs, use of funds and tax-exempt status, if any; the percentage of fundraising that goes toward programs and the percentage used for administrative costs; and more. Visit the BBB Wise Giving Alliance’s website at www.bbb.org/charity for helpful tips.



What's the Diff?

Charitable lead trust vs. charitable remainder trust

They're opposites. The latter pays sums to private individuals each year for a term of years or for life, with the balance of the trust property going to charity thereafter. A charitable lead trust, on the other hand, pays income to a charitable organization for a period of years, after which the trust property is distributed to the selected private individuals.



After your lifetime and that of any surviving beneficiary you have named, the balance in the trust is paid to your chosen charitable organizations.

A retirement unitrust offers you the same tax benefits described earlier. For example, for each year you contribute to the unitrust, you get a money-saving income tax charitable deduction for a portion of the current value of your gift. You can also contribute appreciated securities with the same advantages.

3

Lead Trust

As previously explained, you can arrange a gift of income-producing property to a selected charitable organization while reserving a life income and taking an income tax deduction for a portion of your contributions. You can also reverse the process; that is, you can give income to a charity for several years and provide that the trust's balance will then go to your children and/or grandchildren. They will receive the trust assets free of federal gift and estate taxes or at least with those taxes greatly reduced.

4

Retained Life Estate

You can live in your home but give it to a charity and receive a charitable deduction. This arrangement is technically called a gift of a remainder interest in property. In essence, you retain a life estate.

It works like this. Assume you want to continue using your personal residence for life. You may also want a survivor (perhaps your spouse) to enjoy life occupancy. But ultimately you would like a charitable organization to receive the property.

By deeding your home to the organization now, subject to your right to live in it, you can obtain a sizable current income tax deduction. The amount depends on the value of the property and your age (and the age of any other person given life use).

Did You Know?

The retained life estate charitable deduction is also available for a farm, vacation home, condominium or stock in a cooperative housing corporation if it is used by you as a personal residence.



quizfive

Select the answer you believe is correct. You'll find the key below.

5 Charitable Gift Annuity
The charitable gift annuity pays you a fixed amount for life. You make a gift of money or securities to the charity of your choice, which then agrees to pay you a set amount for life. (The charitable gift annuity option isn't available in a few states or from some organizations.)

The payout rate you receive is determined by your age and the age of any other person you name to receive the payments at the time of the gift. The rate remains constant once you make your gift. The older you are, the higher the rate you can secure when the contract is signed.

For two lives, the rate paid is slightly lower because the period of payment likely will be longer.

Assuming you itemize deductions, you can take a charitable deduction for part of the value of your gift when you file that year's federal income tax return. A portion of each gift annuity payment may also be income tax-free throughout your life expectancy.

There is a taxable gain when a gift annuity is funded with appreciated property. You can avoid or reduce this tax by giving cash or high cost basis property. With appreciated property, the capital gain is not taxed in a lump sum, but usually taxed ratably over your life expectancy as lower capital gains income.

6 Deferred Payment Gift Annuity
Instead of securing an immediate payment under a gift annuity, you can have it deferred until a later date, such as the date of your retirement. You make the contribution now, securing a current income tax charitable deduction. The charitable organization agrees to pay you a set income for life, starting at any date you choose.

This arrangement is especially advantageous if your tax bracket is higher now than you assume it will be later. In addition, the future annual payout rate and your income tax deduction are considerably higher than with an immediate payment gift annuity.



- 1. A retirement plan that allows you a charitable deduction is**
 - a. an IRA.
 - b. a 401(k) plan.
 - c. a unitrust.
- 2. A portion of the sum paid each year from a charitable gift annuity may be**
 - a. tax-free.
 - b. double taxed.
 - c. deferred.
- 3. To get a current tax deduction, your life income gift must be**
 - a. revocable.
 - b. amendable.
 - c. irrevocable.
- 4. A charitable remainder annuity trust pays the beneficiary**
 - a. a percentage of market value.
 - b. a fixed dollar amount.
 - c. its net income.
- 5. The greater the annual payout of a charitable remainder trust,**
 - a. the greater the deduction.
 - b. the smaller the deduction.
 - c. the higher the capital gain.
- 6. You can get a current income tax charitable deduction for your home if you**
 - a. deed it to a charitable organization.
 - b. will it to the IRS.
 - c. move out now.

PEPC-J • The information in this publication is not intended as legal advice. For legal advice, please consult an attorney. Figures cited in examples are for hypothetical purposes only and are subject to change. References to estate and income taxes include federal taxes only. State income/estate taxes or state law may impact your results.