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GENERAL ESTATE PLANNING TERM DEFINITIONS

TRUSTS:

1. Revocable Living Trusts

    1. Simple Husband & Wife - Long term marriage, no children from separate marriages, total estate less than the federal estate exemption amount (currently $2 million - may be changed, may drop back to $1 million). Upon the death of the first spouse, very little administration is required, (retitle all assets in name of Surviving spouse as Sole Trustee; file Affidavit-Death of (deceased spouse) for real property to show Surviving Spouse as sole Trustee; but trust remains revocable, amendable and fully under the control and disposition of the Surviving Spouse.

    2. A/B Trust - Good for estates over the Federal exemption amount, second marriages with children from previous marriages (allows the decedent's share to benefit the surviving spouse during his or her lifetime and then pass to the decedent's beneficiaries upon the surviving spouse's death). On death of first spouse, the B Trust (Below ground spouse's share) becomes irrevocable - need Tax ID #, have to file fiduciary tax return (Form 1041) each year, have to allocate the decedent's share of the estate to this trust (which cannot exceed the Federal Exemption Amount without incurring a tax). A Trust (Above ground spouse's share) remains revocable and amendable - use Surviving spouse's SS# on assets and for reporting on Tax form 1040.

    3. Disclaimer Trust – This is a hybrid A/B. It requires affirmative action to DISCLAIM all or part of the assets of the deceased spouse within nine months of the date of death. If disclaimed, then the trust is managed similar to an A/B. If no disclaimer is executed, then it continues as a simple Husband & Wife trust. This is a good trust where there are no children from previous marriage, but assets might be over the

Federal Exemption amount to allow a "second look" based on what that amount might be at the death of the first spouse to allow proper tax planning.

4. A/B/C or A/B/Q trust. (QTIP) This is for larger estates, or where one spouse's assets may exceed the federal exemption amount. The C or Q trust (terms interchangeable) is a second irrevocable trust into which the excess assets of the deceased spouse may be placed, often referred to as a QTIP (Qualified Terminable Interest Property) trust - a device permitted by the Internal Revenue Code to allow the property to be used exclusively for the benefit of the surviving spouse during his or her lifetime, but still pass to the deceased spouse's beneficiaries after Surviving Spouse's death. This is a device intended to avoid any taxes on the first death. For larger estates, because the Federal Estate Tax is progressive, it might be wiser from a tax planning strategy to permit the Surviving Spouse to disclaim some or all of the property passing to the QTIP trust and actually incur a tax on first death - but at the lowest marginal rate. In that case, you might have an A/B/C/D trust - the D trust providing where the Disclaimed assets would go - generally either held for the surviving spouse or distributed outright to the Deceased Spouse's other beneficiaries.

5. Special Needs Trust: This is a trust for benefit of a beneficiary who is or may need to be on public benefits. If properly drafted, it does not count as an "available resource" for purposes of determining eligibility for programs such as SSI or Medicaid. There are two major types - A Third Party Trust or a First Party Trust.

A. - Third Party Trust - It may be created by the parents or other family members as part of their own estate planning documents: "I leave x% of my estate to the Trustee of the John Doe, Jr. Special Needs Trust fbo John Doe, jr." or as a stand alone Trust - The John Doe Jr. Special Needs Trust. This type of trust, created by a third party using the third party's funds (i.e. - not using the Disabled Person's (DP) assets) is intended to "supplement and not supplant" public benefits, and can pass to other beneficiaries upon the death of the DP.

B. - First Party Trust. It may be created by one of four entities using the funds of the disabled person - such as where the disabled person (DP) received an inheritance outright that will cause him or her to lose public benefits, or make them ineligible, or where he DP received a litigation or malpractice award. This type of trust is allowed under Federal law, often referred to as a d4A trust (for the code section governing it) and may be created by 1. Parents; 2. Grandparents; 3 Conservator or 4. The Court. The "penalty" for allowing the DP's assets and eligibility for public benefits to be preserved is that whatever remains in the trust on the death of the DP must first go to pay back the State for benefits it has provided. SSI has no recovery, but health care benefits provided by the State are subject to "pay back" provisions. Anything remaining after "pay back" can go to other beneficiaries, but the trust must be carefully drafted; some jurisdictions interpret "sole benefit," a requirement of the statute, very narrowly - and may require it go to "heirs at law" as opposed to specifically named beneficiaries. Check with a competent attorney with experience in this area in your state. We usually give the DP what is called a Limited Power of

Appointment, exercisable by Will, thus allowing a method for the DP to name the beneficiaries (or change from time to time) without running afoul of the "sole benefit" rule.

6. Charitable Remainder Trust – (may also be referred to as a "gift annuity trust.") Where you can leave assets that will go to the charity at the death of the Trustors, but will provide income to the Trustor/s during his or her/their lifetimes. It provides a charitable benefit for the present value of the charitable bequest in the year gifted. It's often referred to as a way to "make money by giving it away." For example - many organizations that rely on donations (such as the Zoological Society) will provide for "gift annuities" and a side benefit is a lifetime membership with lots of additional donor benefits.

7. Irrevocable Life Insurance Trust. This is a way to provide life insurance benefits (liquidity) to your beneficiaries without the value of that insurance being tacked on top of your estate for federal estate tax purposes. A new policy is best, but there are several technical requirements and requires an attorney versed in tax law to properly set it up.

8. Continuing Trust. A generic term that usually refers to an irrevocable trust that continues for a beneficiary named in an existing trust. Used in any situation where the Trustor wants to benefit a beneficiary but without giving them control of the corpus (as opposed to outright distribution). Examples: Minor children, spendthrift beneficiaries, substance abuse beneficiaries, to provide protection of assets in event of divorce.

OTHER MISCELLANEOUS DOCUMENTS:

Power of Attorney - A document in which the Principal gives the power to another person (the Agent, etc) to handle the Principal's affairs under certain circumstances - often in the event of the disability of the Principal, but may be more temporary, such as a Power of Attorney from one spouse to the other to allow the sale or purchase of property (such as on transfer) or a Power of attorney given to a family member with whom minor children are going to be residing for a period of time - to allow the authorization of emergency medical treatment. In most states you will need two Powers of Attorney - one for asset management and the other for health care. The agents may be the same or different.

Durable Power of Attorney for Asset Management - Durable means it is valid even if the Principal becomes incapacitated. That's good - since that's generally the purpose of establishing one. The agent is often the other spouse, and then other trusted individuals. (Should consider the agent's ability to handle financial matters - not just name "the oldest son, or someone similar." This person will be making financial decisions, so don't choose someone who can't balance his or her checkbook. May be the same person who has been named as Trustee - but the duties are definitely

different – they have to understand which "hat" they are wearing. Agent will usually make financial elections - handle annuities, Medicare decisions, survivor benefit issues, claim insurance proceeds, etc. (financial decisions relating to all assets or income that are not titled in the trust.)

Durable Power of Attorney for Health Care (HCPOA)– The agent selected by the Principal to make health care decisions when the Principal is no longer able to "give informed consent," such as whether to withhold or withdraw life support, whether to pull the plug, what kind of care the principal is to receive and where they are to receive it (home, nursing home, assisted living facility, etc). It is very important that this document reflect what the principal's wishes are as much as possible: whether and under what circumstances the principal would or would not want life support used, how they would want certain "terminal" illnesses to be handled, whether they want to be buried or cremated and if so where. If any pre-arrangements have been made, the HCPOA should list the name and contact information; if the principal wants to be an organ donor (or not) that should be spelled out. The Principal needs to discuss his or her health care preferences with the selected agent, make certain that person is both willing and able to serve and will carry out the Principal's wishes. For this selection, it is preferable to have someone as close as possible - you don't want to have immediate health care decisions delayed until someone can fly across country.

Will - This is a document that must be drafted and witnessed according to the requirements of the state of residence. It reflects the Testator's wishes for the disposition of his or her property. If the assets that are to be distributed under a Will exceed the State's small estate amount (for example, $100,000 in CA) then a probate must be opened. In some states probates are much more expensive and time consuming. Probate is the legal process, differing somewhat in many states in complexity and cost, that transfers the title to the assets of a deceased person to the decedent's named beneficiaries, after making sure all the decedent's debts have been satisfied.

ADDITIONAL TERMS:

Trustor/Grantor/Settlor – Different areas use different terms, but they are essentially interchangeable. This is the person or persons who create the Trust.

Trustee – The person or persons (or entities - such as a bank or trust company) who are named to manage the assets of the trust. Generally in a husband and wife trust, H&W are the original Trustees, the Surviving Spouse is the Successor Trustee, and then someone should be named to manage the trust after the death of both spouses. In some cases, if multiple trusts are created on the death of one spouse, different people may be named as trustee of the various trusts, particularly in second marriage situations. A trustee will hold "legal title" in a fiduciary capacity, but will hold the assets for the benefit of the beneficiaries.

Co-Trustee – Where two or more persons are named as trustees.

Successor Trustee – The persons or entities named in succession to act if the Trustee named

before them is unable to act for any reason.

Beneficiaries – These are the persons who are named in a decedent's Will to receive the decedent's property after decedent's death or the persons entitled to the beneficial interest in the trust at any given time. For example, in a typical H&W trust, H&W are the initial beneficiaries; After the death of first spouse, surviving spouse (and perhaps children) are beneficiaries; After the surviving spouse's death, the trust will provide who benefits - either with an outright distribution, or through the use of a continuing trust. A beneficiary may also be named in other types of instruments - such as the beneficiary of your insurance policy, of your IRA, of a POD (payable on death) or TOD (transfer on death) account, just to name a few.

Heirs-at-Law - The persons who take a decedent's property under the state's Intestacy laws. Generally it follows a specific chart composed of spouses, issue, parents, issue of parents (aunts, uncles, cousins). May differ slightly from state to state. Legally adopted children generally qualify, but step children normally do not.

Issue – A term meaning lineal descendants - children - grandchildren - great grandchildren, etc. Again, most state laws include legally adopted children, but not stepchildren.

Trust Protector or Referee - A person or entity who may serve a variety of purposes. For a disabled person, they may be required to receive and review the accounting of the Trustee, they may have the power to remove a trustee who is not performing properly, or who shows hostility to the beneficiary; if two children are named as successor co-trustees, the referee may be the tie breaking vote in the case of disagreement. NOTE: You want to give serious consideration to naming one child of several, or two or more. Beware the Squabbling Sibling Syndrome.

Principal – The person who creates a Power of Attorney.

Agent, Power of Attorney (POA), Attorney in Fact (AIF) (interchangeable)- The person who is named to act on behalf of the principal under a power of attorney.

If Co-agents are named, it must be spelled out in the document whether the agents are required to act in concert or may act independently. Many financial institutions will require they act in concert - so keep this in mind if selecting Agent 1 on the west coat and Agent 2 on the east coast, or if selecting Child 1 and Child 2 who can't agree on the time of day.

Testator - the person who makes a Will.

Executor - the person named in a Will to administer the will (similar to the Trustee of the Trust). Note, unless the estate qualifies for some small estate procedure, usually requires Court authority, i.e. Letters Testamentary.

Intestate – When an individual dies without a Will or Trust, his or her property will pass to the persons named under the decedent's home state "Intestate Succession" laws or laws of "Intestacy." It may not be the persons or in the order the decedent would wish, but if you

don't control your estate plan - the state will control it for you.

Incapacity - The condition of an individual of being unable to properly manage his or her financial resources or to make "informed" medical decisions regarding his or her care. Generally the determination of what constitutes "incapacity" should be spelled out in all estate planning documents - because some may consider you incapacitated before you agree. Some common, though not necessarily best, "triggers" are "In the written opinion of my doctor;" "In the opinion of two of my three children;" "In the written opinion of my attorney and my CPA - named." There may be problems with all of these, so the "trigger" should be very carefully considered.

Power of Appointment - This is a power given to a spouse or a third party permitting the holder of the power to "appoint" the decedent's property and perhaps change the distribution set forth, for example, in the individual's trust. It is a powerful tool, so must be used with care, and the limitations must be spelled out carefully. Often the power is limited to "heirs or named beneficiaries" of the individual giving the power. Used to provide for Changed Circumstances. Example - the decedent's trust may provide that upon the death of the Surviving Spouse, Trust be will be distributed in equal shares to Child A, Child B and Child C outright and free of trust. After decedent's death, Child C is involved in a disabling accident and has qualified for public benefits. The holder of the Power of Appointment can "amend" the trust to provide that C's share will go to a Special Needs Trust. Other circumstances where may be helpful - substance abuse beneficiaries, spendthrift children, greedy or disfavored spouses of named beneficiaries, or the need to protect the assets in the event of a beneficiary's divorce. (May want to change from an outright gift to one that holds the property held in a continuing trust, under specified terms and limitations, to protect against the CHANGED CIRCUMSTANCES.)

HIPAA – a federal statute that went into effect about three years ago that is intended to provide privacy protection against the unauthorized disclosure of an individual's medical information. One of the perhaps unintended negative side effects is the actual or at least perceived problem of a doctor being unwilling to sign the Incapacity Declaration for a patient that would allow the agent to take over the Principal's affairs or the Successor Trustee to take over management of the trust. A possible solution is to include a Waiver of HIPAA in your estate planning documents, authorizing your physician to release this information to the person named in the documents who is referred to as the Personal Representative in the statute.

Joint Tenancy – This is a form of holding title that allows property to pass to the surviving tenant without probate. Usually requires merely the filing of an "Affidavit of Death" of the deceased owner. It's a very simple way to pass, for example, the family residence to the surviving spouse - property is held "H & W as joint tenants with the right of survivorship." In community property states, this form of title may result in negative tax consequences - the property will receive a step up in basis to the fair market value as of the date of death only for the decedent's interest; whereas in community property states, if title is held "H&W, as community property," then both halves will receive a stepped up basis. Another risk is that both spouses are killed in the same accident, perhaps both estates will now require probate,

or the entire estate might go to the family of the spouse who survived a little longer. Usually not the intended distribution in a second marriage.

Community Property - A form of holding title in community property states only. Each spouse can bequeath his or her interest to a third party by will or trust, but if it goes to the surviving spouse (via Will, Trust or Intestacy), it can pass to the surviving community spouse without probate.

Tenants in Common - A form of holding title in which each owner holds an undivided interest in the same asset. Each owner handles the disposition of his or her interest during life or upon death; there is no "survivorship" interest to the other tenant (owner). This is commonly used when siblings own property together (perhaps a vacation home); or when Mom and Dad and one of their children purchase property together. Tax consequences, stepped up only as to the interest of the deceased tenant for his or her transferee.