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SOME INFORMATION on ESTATE PLANNING

Before you begin the process of estate planning, you need general background. It is not enough to simply have a will; you must understand how it fits into your life goals and financial plans so that you can be smart about strategy and make good daily life decisions. Your consultation will be more useful to you if you prepare by reading this information.

ESTATE DOCUMENTS YOU MAY USE

A brief summary of documents that can accomplish your estate planning goals:

1. WILL

Wills control what happens in probate -- they do not avoid probate. A will bequeaths property you own when you die to named beneficiaries. It cannot control property subject to a right of survivorship or that does not terminate at your death. A will should be drafted in general terms to control whatever assets you own at your death, and to cover whatever beneficiaries are living at your death, so you do not have to revise it frequently. We do witnessed, self-proving wills that can be presented for probate without the testimony of family, friends and witnesses. It is still a good idea to be alert to easy ways to avoid probate while still achieving your goals. Each individual must have their own will.

2. LIVING TRUST

A living trust is a tool to achieve specific estate planning goals. It has a settlor (you), one or more trustees (also frequently you at first) who manage the assets in the trust according to the terms you set out, and one or more beneficiaries (also potentially you during your lifetime) who receive the assets in the trust according to the terms you set out. It is in effect during your life as well as after your death. A living trust is used to manage assets for your benefit if you are disabled, or for the benefit of your dependents (such as children) if you are not able to handle these affairs yourself. Assets in a trust are not subject to your will and do not go through probate at your death.

3. GENERAL, DURABLE POWER OF ATTORNEY FOR FINANCIAL MATTERS

Everyone should have a power of attorney that appoints a trusted person (or several) as their agent to handle business for them, especially when they cannot manage themselves. When

you execute a general, durable power of attorney, you authorize your agent, to carry on any business matter for you. **A power of attorney is only effective while you are living.** Its main purpose is to allow an agent to work for you if you are sick.

4. HEALTH CARE POWER OF ATTORNEY

You may appoint someone to make health care decisions if you are unable to decide for yourself. By executing a Health Care Power of Attorney, you appoint an agent, and one or more alternates, who are authorized to consent to or refuse any health care that may be considered for you. You may indicate your general wishes for health care and may make this power limited or broad.

5. LIVING WILL

A Living Will allows you to indicate to your family and health care providers your wishes for care if you are terminally and incurably ill or in a permanent vegetative state. It addresses the use of life support measures and artificial hydration and nutrition (tube feeding). These directives may be in addition to or instead of a health care power of attorney. A Living Will expresses a decision; a Health Care Power of Attorney delegates decision-making to someone who understands your wishes. We customarily condense the two into one document.

ANSWERS to FREQUENTLY ASKED QUESTIONS

WHAT IS PROBATE?

Probate is a Court process of transferring assets from a person who has died to the persons or entities entitled to receive all the assets. It includes paying the debts of the deceased person. Writing a will does not eliminate probate. However, planning your estate involves deciding what you want to have pass under your will through probate to named heirs and what should pass to beneficiaries in other ways outside of probate.

WHAT PROPERTY WILL PASS UNDER MY WILL?

All property that is titled in **your name alone** will be disposed of by your will: a bank account, stock, real estate, automobiles, household items and similar items. If you own an undivided interest in property with another, your undivided interest will pass under your will, but not if the property you own with another is titled joint with right of survivorship.

WHICH ASSETS WILL <u>NOT</u> PASS UNDER MY WILL?

Property titled in joint names with right of survivorship will pass to the surviving joint owner. For instance, homes owned by a married couple usually go to the survivor. Joint bank accounts are generally titled with a right of survivorship.

- Life insurance will go to the named beneficiary(ies). These funds can go to a trust if you set one up, avoid probate, but have specific management instructions.

- Pension, retirement or other employee benefits will go to named beneficiary(ies). You do not want these funds to pass under your will for the best tax benefits. They can also be paid to a Trust, especially if you have young children.

- U.S. Savings Bonds held in joint names will go to the survivor. Those payable on death to a named beneficiary will go to the named beneficiary.

However, if the named beneficiary in any of the above examples is "your estate" or your "executors and administrators," then this property will pass under your will.

WHAT ARE CONSIDERATIONS IN DECIDING HOW TO BEQUEATH PROPERTY?

Goals. Your first step should be to think carefully about your goals and how the terms of your will can accomplish your goals.

Strategies. It is **not** necessary, or even good, that you name or describe each item that you expect to pass under your will. Your assets can be described by groups, categories or in any other way which adequately describes your property. It is also possible to leave all your property or certain categories of it, to more than one beneficiary by providing that each beneficiary is to receive a fraction or percentage of all or any category of property.

If you would like for a particular beneficiary to receive a specific amount of money, such a provision should be clearly expressed in your will. However, because your estate may increase or decrease substantially between the time you sign your will and the time of your death, you may wish to consider whether this amount of money should be limited by a percentage of your estate. For example, assume your estate is worth $50,000.00 and you wish to leave a beneficiary $500.00. Five Hundred Dollars is 1% of your estate. If your estate should shrink to $25,000.00 by the time of your death, the bequest of money may be more than you would have intended under the circumstances. If, however, your bequest is made in terms of the lesser of $500.00 or 1% of your estate, then the bequest would shrink proportionately with the total assets.

WHAT ABOUT PERSONAL AND HOUSEHOLD EFFECTS?

In dealing with your personal effects, household goods, etc. (which includes furniture, appliances, silverware, china, wearing apparel, automobiles, etc.), we frequently recommend leaving all such property to a surviving spouse and alternatively to children, grandchildren, etc., rather than specifying in your will that such and such item goes to so and so, etc. You can always write up a memorandum to keep with your will that specifies whom you want to receive particular items within the group that you have named in your will. Although such a memorandum is not legally binding, it is usually persuasive for your family members. It gives you the advantage of being able to change it any time without amending your will and avoids the necessity of obtaining a receipt from each beneficiary. (There may also be additional tax consequences of these specific bequests.)

WHAT ABOUT MY DEBTS?

All your debts that come due will be paid from the assets of your estate. However, if you own land subject to a mortgage, unless you provide otherwise in your will, the person to whom

you leave the land takes the land subject to the mortgage. The executor will not pay off the mortgage. If this is not what you desire, you may direct the executor to pay the mortgage out of the other estate assets. Your debts reduce what your heirs receive, but they do not have personal responsibility for your debts.

WHO HANDLES MY ESTATE?

The "executor" handles your estate, which means that this person does everything necessary to carry out the intentions of your will, complete your business affairs, and satisfy court requirements. More specifically, the executor will collect your assets, pay your debts, compute and pay any taxes that are due and distribute the remainder of your property to the beneficiaries named in your will. This usually takes six months to a year.

In your will, you will name the executor and usually an alternate executor. Many people name their surviving spouses and alternatively, adult children, but it can be any competent adult. The alternates are named in the event that, at the time you die, the primary executor cannot, or will not for some reason, serve. You can also, if you wish, name more than one person to serve as co-executors, or name a financial institution or trust company as a corporate executor.

It is not necessary that your executor, if an individual, be a resident of North Carolina. However, this is generally a good idea for practical reasons. It can be inconvenient for the out-of-state executor to spend a lot of time in North Carolina and to make repeated trips to take care of details. Also, the out-of-state executor will be unfamiliar with the necessary services offered locally. There may also be an expense to your estate to post a bond for this out-of-state executor

WHAT ABOUT GUARDIANS FOR MY CHILDREN?

Your will is the best place to name individuals you would like to physically take care of minor children should you die before your children are grown and on their own (legally, at age 18). You should pick one or more persons you would trust with your children, and equally important, people who are willing to take on the tremendous responsibility of taking care of your children. Whatever you do, contact these people and get their permission before you name them in your will.

WHAT ABOUT THE MONEY FOR MY CHILDREN?

Should both parents die before minor children are grown, there can be severe money problems for the children and the guardians. Money going directly to a child from your estate will be supervised by the court until the child reaches the age of 18. It is a burden on the guardian to be responsible for your children and also to be accountable to the court for all expenditures from your children's money. Then, at age 18, your children will get all their money, no strings attached. * The financially immature child often squanders the inheritance, leaving the child with no money and no real long-term benefit. You should, therefore, have some type of trust to address these problems. We will discuss this in more detail when we meet if you have minor children.

SOME DEFINITIONS OF TECHNICAL TERMS

(a) **Bequest, bequeath** - A bequest is a gift by will of money or personal property (excluding land). To bequeath means to make such a gift.

(b) **Codicil** - A codicil is an amendment to a will which changes the will in some manner. It is a separate document and must be executed with the same formalities as a will.

(c) **Devise, devisee -** A devise is a gift by will of property. The term traditionally referred to gifts of land, but now it generally refers to any gift by will. A devisee is the person to whom property is given by a will.

(d) **Descendants –** Descendants are lawful blood and adopted descendants, whether children, grandchildren, great grandchildren, etc. We can define "descendants" to specifically include or exclude step-children, etc.

(e) **Legacy** - This term is frequently used as a synonym for bequest, but technically means a gift by will of money.

(f) **Lapsed legacy or devise** - When a beneficiary under a will dies before the person making the will, the gift lapses, which means that it does not pass to the deceased person or his estate. There is an exception: if the surviving descendants of the beneficiary would have been heirs of the person making the will, they will step in and take the bequest.

(g) **Per stirpes** - This is a Latin term which, when used in a will, means that if a beneficiary of a will dies before the testator leaving surviving children, those children will take their deceased parent's share under a will.

(h) **Residuary estate** - The residuary estate is that portion of your total estate covered by a residuary clause in your will. The residuary clause of your will disposes of all your property not disposed of earlier in your will. In other words, after you have made specific gifts, a residuary clause normally provides that you leave "all the residue" of your estate to one or more beneficiaries.

(i) **Testator/Testatrix -** The term for the man/woman who is making a will.

USING TRUSTS to ACCOMPLISH YOUR GOALS

Sometimes, when you are discussing your estate planning goals, your lawyer will suggest that you create a revocable living trust as one of your estate planning tools. A revocable living trust is a legal entity separate from you that can hold assets and provide for their management. A Trust is a tool we can use to accomplish your goals.

There are many different types of trusts. What follows are some common types of trusts that we draft in this office.

PARTIES TO A TRUST

There are different roles in a trust, and these roles are played by various individuals or "parties" to a trust. An individual may serve in more than one role in the same trust.

There are three essential parties to a trust – **settlor**, **trustee** and **beneficiary**. (There may also be another party, called a **trust protector**, but this party is not required and is not commonly found in simple trusts.)

The **Three Essential Parties** are:

1. **Settlor.** The settlor is the party (or parties) who creates the trust. Settlors are also called "grantors," "trustors" or "makers." Wallis Law Firm documents use the term "settlor."

2. **Trustee.** The trustee is the party who administers the trust and carries out the settlor's intent. The trustee can be one individual, more than one individual (co-trustees), or an institution (like a bank or trust company). The trust can also name alternate or successor trustees:
   - Co-trustees are two or more parties who act as trustee at the same time; and
   - Successor trustees (sometimes also called alternate trustees) step in as the acting trustee when the previously acting trustee is no longer able or willing to serve as trustee. Depending on the language in the trust, successor trustees can act together as co-successor trustees, or successively (each succeeds the prior).

   If there are co-trustees, or co-successor trustees, the language in the trust determines whether each can act alone or whether they must act together.

   If your property is titled or held in the name of a trust, only the acting trustee of the trust can handle matters concerning that property.

3. **Beneficiary.** The beneficiary is the person or persons for whose benefit the trust was created. Sometimes there is only one beneficiary named, but more often there are multiple beneficiaries. Some beneficiaries are "primary beneficiaries," which means they have some entitlement to the assets in the trust without any necessary pre-conditions that must come to pass. Trusts also usually name "contingent beneficiaries" (also called "secondary beneficiaries"), who are not entitled to the assets or benefits of the trust until some specified condition or events occurs (often the death of one or more primary beneficiaries).

REVOCABLE TRUSTS AND IRREVOCABLE TRUSTS

Trusts can be divided into two major categories: **revocable** and **irrevocable**. Whether a settlor creates a revocable trust or an irrevocable trust depends on the settlor's purpose for creating the trust.

- **Revocable Trust:** A revocable trust, the most common type of trust, may be modified, amended or revoked (dissolved) by the settlor at any time. Sometimes in the trust, the settlor grants another individual the authority to modify, amend or revoke the trust. A revocable trust automatically becomes irrevocable at the death of the last surviving settlor.

- **Irrevocable Trust:** An irrevocable trust generally cannot be modified, amended or revoked by anyone other than the courts. A settlor may create an irrevocable trust for tax purposes or for other special purposes. One common special purpose trust is a **special needs trust**.

OTHER TRUST TERMS YOU MAY ENCOUNTER

- ***Inter Vivos* Trust.** The term "*inter vivos"* is Latin and means "between the living." An *inter vivos* trust is simply a trust created by the settlor during his or her lifetime. An *inter vivos* trust is more commonly called a "**living trust.**"

- **Grantor Trust.** A grantor trust is a living trust in which the settlor retains control over the trust property or its income to the extent that the settlor is taxed on the trust's income. In a grantor trust, the settlor is typically the initial trustee and the beneficiary, and family members are often secondary beneficiaries. The term "grantor trust" is officially defined in the Internal Revenue Code ("IRC").

  Many revocable living trusts are grantor trusts. What this signifies is that the trust may use the Social Security Number ("SSN") of one of the living settlors as its Tax Identification Number ("TIN"). Income earned by the trust would then be reported on the settlor's personal tax return. Once the last surviving settlor of the trust dies and the trust is no longer revocable, the trustee will need to obtain from the Internal Revenue Service ("IRS") a unique TIN for the trust (called an "Employer Identification Number" or "EIN").

- **Testamentary Trust.** A testamentary trust is a trust that an individual creates in a will. The individual who creates the will is called the "testator," and this same individual is also known as the "settlor" of the trust created in the will. Because the trust is created by will, it does not take effect until the testator/settlor dies. A testamentary trust is also called a "**trust under will**."

- **Special Needs Trust.** A special needs trust is a trust established for persons with disabilities (the "trust beneficiary") that helps provide certain limited goods and services for the beneficiary, maintaining the trust beneficiary's eligibility for public benefits. Special needs trusts are governed by the laws of the state where the beneficiary resides and are drafted to comply with the rules of federal needs-based benefits programs for people with disabilities. The beneficiary cannot receive ordinary support from a special needs trust so their usefulness is not as great as many people assume.

DO I NEED A TRUST? FACTORS INFLUENCING YOUR DECISION TO CREATE A TRUST

Whether creating a trust would be useful, depends on your specific estate planning goals. A trust is simply a tool for accomplishing goals. There are many factors that may influence your decision to create a trust. Some of these factors are as follows:

Asset Management in the face of Aging or Worsening Health of Settlor

A trust can be useful for ensuring management of your assets *during your lifetime*, especially as you are aging or if you face increasing incapacity due to a long-term or chronic illness. While you

can certainly appoint an agent in a power of attorney to handle your affairs if you are unable to do so, the agent operates only under a duty of loyalty to act in your best interests. A power of attorney does not provide the agent with specific instructions on how to manage your financial affairs. **This can be accomplished more readily and powerfully with a trust.**

If you set up a trust to ensure management of your assets during your lifetime, you may serve as the initial trustee so you maintain administrative control of your assets for as long as you are able. After establishing the trust, you would need to transfer your assets to the trust. You can do this by retitling accounts from your name to the name of the trust. If you expect to be the beneficiary on someone else's accounts or life insurance policies, you should request that they change the beneficiary name from your personal name to the name of your trust.

Minor or Young Children

In North Carolina, a guardian must be appointed for minor children who lose both their parents. However, a guardian does not have unfettered use of the parents' assets that are left directly to the minor children in a will. Distribution and use of assets bequeathed directly to minor children must be supervised by the Clerk of Court until the child reaches the age of 18, at which point formal guardianship ends and the assets are turned over to the 18-year old child.

Rather than leaving assets directly to minor children in a will, another option is for **parents to create a living trust with their children named as beneficiaries**. Parents can then leave the property in their estate to the trust. Alternately, during their lifetimes, parents may title some, or all, of their property in the name of the trust, rather than in their own names, so these assets bypass their probate estate entirely.

In the trust, the parents can appoint a trusted person (or institution) as trustee, and this party can administer the trust assets in accordance with the parents' wishes as stated in the trust. For instance, the trust can state that the assets in the trust should be used to pay for education if not otherwise needed for the children's care and maintenance. The parents can also direct the trustee not to distribute the remaining funds held in trust until each child (or all the children) reaches a certain age and has more wisdom and maturity to manage the assets. **One of the biggest advantages of leaving assets to a trust, rather than directly to minor children, is that court supervision is not required when assets are left to a trust.**

Individuals with Disabilities

Parents, grandparents, siblings and other relatives often create a Trust, or perhaps a special needs trust for a child or adult family member with a disability (the beneficiary). Sometimes these trusts are set up by the beneficiary's guardian or the court.

If the trust is properly drafted and administered, the trust will allow the beneficiary to benefit from the trust while retaining eligibility for federal needs-based programs such as Supplemental Security Income (SSI), Medicaid, Section 8 housing and food stamps. Any income to the disabled person, which may reduce or disqualify the person for federal benefits, is placed in the trust, and these assets are not included in their benefits eligibility calculations.

If you plan to make lifetime gifts or bequests at death to a person with disabilities, **it is often preferable to make the gifts or bequests to the person's special needs trust to prevent disqualifying the person from public benefits**. However, keep in mind that only certain

distributions from a special needs trust are permissible. Non-permissible distributions will reduce or eliminate eligibility for public benefits.

General Comments About Whether You May Want a Trust

There are many other factors that may influence your decision to create a trust. In general, however, creation of a trust can provide:

- **Management during your lifetime.** If you are unable to manage your assets, or you foresee a time in the future when you will not be able to do so, a trust may be a useful tool to provide a legally binding roadmap for someone else to manage your assets during your lifetime.

- **Management after your lifetime.** If you have beneficiaries who are unable to manage assets, a trust may be a useful tool to provide a legally binding roadmap for someone else to manage assets for your dependents or other beneficiaries.

- **More efficient estate settlement.** A trust may be a more effective way to distribute your assets after your death. For instance, while you can specify in your will *who* should receive your property at death, in a trust you can also instruct your trustee as to *when* the beneficiaries receive the assets and *under what conditions*.

- **Easier estate settlement.** Assets held in a trust, rather than in your own name, do not become part of your estate after your death and do not have to go through probate. This may make the assets available more quickly and easily to your beneficiaries after your death.

- **Privacy.** Unlike the provisions in your will, the terms of a trust are more private and do not become public record.

If your estate is simple, however, and you have no minor children or grandchildren, and your intangible assets, such as bank and securities accounts, are either jointly titled with right of survivorship or have designated beneficiaries, you may not need the extra complication of a trust.

FUNDING THE TRUST

Once you create a trust, you need to ensure it is funded during your lifetime, or will be funded at your death. "Funding a trust" means putting your property into your trust.

Trust Is Funded at Your Death

- **Testamentary Trust.** If you have a testamentary trust in your will, your trust is created upon your death and is funded when your personal representative (either your executor or administrator) distributes estate assets to the trustee.

- **Living Trust.**
  - If you have created a living trust, your will would generally include a "pour over" provision in your will in which you bequeath the residue of your estate property to the trust. A simple pour over provision might look something like: "I leave the rest of my estate not otherwise distributed to the XYZ Trust." Upon your death, the personal representative of your estate transfers the applicable assets from your probate estate to the trustee of the trust as part of

settling your estate. Your trust lives on according to the terms of the trust, and your trustee or successor trustee takes over its administration.

- As mentioned above under **Factors Influencing Your Decision to Create a Trust**, if you are the initial trustee of your trust, you can title (or retitle) your personal assets (bank accounts, securities accounts, etc.) in the name of the trust.

- You can also name your living trust as POD (Payable at Death) or TOD (Transfer at Death) beneficiary on your bank, credit union and securities accounts and on life insurance policies. Upon the death of the last surviving owner of the accounts, or the insured on your life insurance policies, the proceeds will be immediately payable to your trust.

Funding Living Trust Prior to Death

If you create a living trust, you typically provide initial funding (even a nominal amount) when you create it and at various times later during your lifetime. If you want to avoid having your assets go through probate, you should make sure while you are living that either (i) your properties are titled in the name of the trust, or (ii) your trust is named as beneficiary.

Bank and Brokerage Accounts. You may wish to title any new accounts you open in the name of your living trust, and also change your existing accounts so they are titled in the name of your trust. An account held in the name of a revocable living trust can use the Social Security Number of any one of the living settlors of the trust, and income on the account is treated as earned by that individual for tax purposes. Keep in mind that once an account is titled in the name of a trust, only the current trustee and any co-trustee has authority to access the account or execute transactions on the account. Your agent appointed in your power of attorney will generally not have access to these accounts unless your agent is also the currently-acting trustee of your trust.

When opening a new account in, or converting an existing account to, the name of your trust, you may be required to execute a **"certification of trust"** in which you, as the trustee, attest to the identity of the current trustee and that the trust is still in existence.

When transferring a brokerage or securities account to your trust, you may also be required to have your signature on the transfer form guaranteed by an officer at your bank or other financial institution under the Securities Transfer Agents Medallion Program (STAMP). This is sometimes referred to as obtaining a "**Medallion.**"

Insurance Policies. If you would like your trust and, ultimately, the trust beneficiaries to receive the proceeds of any life insurance policies you own that are written on your life, you will need to designate the trust as the beneficiary of the policy. As with bank and brokerage accounts, the insurance company may require the trustee to provide, on its form, a certification of trust attesting to the identity and authority of the trustee.

Real (Deeded) Property (land, houses, etc.). If you wish, you can retitle your real property in the name of your living trust while you are living. To do so, you must execute and file a transfer deed. This is particularly useful for land that you own in another state, because if you die owning it in your name, your survivors would need to open another separate probate proceeding for the land in the other state.

MUST I PROVIDE MY ENTIRE TRUST DOCUMENT WHEN DEALING WITH THIRD PARTIES SUCH AS FINANCIAL INSTITUTIONS?

Most states have adopted a version of the Uniform Trust Code (**"UTC"**). Under the UTC, a bank, securities firm, insurance company, or other third party transacting with a trust cannot require a copy of the entire trust document if, instead, the trustee provides a current and properly executed copy of a certification of trust. Most financial institutions have their own "certification of trust" forms that you or other trustees of your trust may complete. In addition, the third party institution may also request (and is permitted to do so) that the trustee provide "excerpts" from the trust that show the name of the trust, the names of the settlors and trustees (including any successor trustees), and the authorities given to the trustee