5 TRUSTS EVERYONE NEEDS TO UNDERSTAND:

SUCCINCTLY EXPLAINED

BY

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ABOUT THE AUTHOR

John Kidwell is the Owner and Managing Partner of the Law Firm of Kidwell & Kent, with offices in Fairfax, Virginia, and Rockville, Maryland. Mr. Kidwell also owns and operates his in-firm commercial and residential real estate title company, Old Dominion Title Services, Inc.

In 2013 John Kidwell was selected by the Registry of Who's Who as a pillar of the community for his work as an attorney and continued dedication to charitable contributions.

In 2014 John Kidwell was inducted as a member of Trial Masters, an elite national organization composed of lawyers with significant courtroom experience. Membership is an indication of a strong commitment to taking clients' cases all the way to the courthouse when warranted. Fewer than 1/2 of 1% of the attorneys in the United States are members.

In 2015, Mr. Kidwell was peer nominated and awarded through the Heritage Foundation as a TOP ATTORNEY IN THE NATION.

In 2016, the Expert Network certified Mr. Kidwell in the TOP 3% of attorneys in America.

In 2017 Mr. Kidwell obtained his Life Health and Annuities, Series 7 and Series 66 Financial Planning Licenses to provide individual and business financial planning services to his clients.

In 2018 Mr. Kidwell was peer nominated and awarded as a top Estate Planning Attorney in America by Lawyers of Distinction and his firm was awarded as a Top Ten Estate Planning Law Firm in Virginia.

Mr. Kidwell is a published author on the topics of law and politics. His books, "Leading by Example: Renovating the American Dream", and "25 Articles on the Law", and others, can be found on Amazon and are available for download. Mr. Kidwell also writes a periodical newspaper column on Real Estate

Law for the "Times Community Newspapers" published in Northern Virginia, and teaches courses in real estate law and wills, trusts, estate and financial planning throughout the area.

The Law Firm of Kidwell & Kent is a general practice law firm with many areas of legal concentration. Mr. Kidwell has over 16 years of experience in real estate litigation and transactions, wills, trusts, and estate planning, business representation, domestic relations, civil litigation, and financial planning. By being able to provide these services, Kidwell & Kent is a law firm designed for the American Family.

John received his bachelor of arts in political science from the University of Mary Washington in 2002 and his juris doctorate from the George Mason University School of Law in 2005.

Mr. Kidwell always keeps philanthropy at the forefront of his endeavors. In 2006 John founded Alternative Fuels for America, a 501(C)(3) charitable organization dedicated to raising funds for the National Renewable Energy Laboratory in order to fund the advancement of clean fuel technologies, specifically alternative fuel sources for automobiles.

In 2011, Mr. Kidwell was a Man of the Year candidate for the Leukemia & Lymphoma Society where he raised tens of thousands of dollars in 10 weeks to fund a cure for cancer.

Mr. Kidwell regularly conducts free legal clinics for Wills for Heroes, the Veterans Administration, local churches and assisted living facilities.

John was also appointed by the Fairfax County Board of Supervisors to the Information Technology Policy Advisory Committee, tasked with advising local government on the implementation and management of information technology services and platforms. Mr. Kidwell served on the Information Policy Advisory Committee from 2011-2013.

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INTRODUCTION

Perhaps you've googled Trusts. And if you have, you're probably one of the millions of Americans who quickly found themselves summarily confused and bombarded with terminology that makes no sense at all. Irrevocable? Revocable? QTIP, Credit Shelter Trusts, Perpetuity Trusts, Generation Tax Skipping? And so on.

There are many different types of Trusts out there, and the terminology that has derived from them only serves to complicate any understanding as to how they operate and exactly what they are designed to accomplish.

What are the different types to trusts? Which ones do you need or might you consider?

Now, to be clear, I believe every estate plan should be scrutinized individually, and that there should be no cookie cutter approach to planning for the efficient transfer or protection of my client's assets- but, that being said, I would like to share with you the 5 Trusts that I have found are of most value to the widest range of clients I have had the privilege of counseling.

The TOP 5 TRUSTS ARE:

1. **THE PROBATE AVOIDANCE TRUST**
2. **THE MARITAL DEDUCTION TRUST**
3. **THE IRREVOCABLE LIFE INSURANCE TRUST**
4. **THE SPECIAL NEEDS TRUST**
5. **THE CHARITABLE REMAINDER TRUST**

First, let's start with what a Trust is and why you might consider it in addition to a Last Will and Testament when planning for your estate.

Most people understand what a Will is. It is a document where you can direct where your assets go when you die. You direct to whom the assets will go, aka your beneficiaries. And you control how much and even when the assets will be transferred.

Well, a Trust is very similar. A Trust is a contract. Think of it as a bucket. In this bucket, you pour in your personal, financial and real estate assets, otherwise known as your estate. Whether they take the form of your home, your cars and personal property, your bank accounts or your life insurance, you pour these assets into the Trust bucket and then, in terms clearly spelled out in the Trust Agreement, you direct to whom your assets will go upon your incapacity and death.

With Trusts, the goal is often to avoid probate, which is to say, the legal administration of your estate through the court system, and/or to mitigate against taxes and protect assets from creditors. A Trust, ultimately, is a mechanism to maintain oversight and control over your assets, and as I always like to joke – a way to govern from the grave.

So, with that quick primer on Trusts, I present to you the first Trust on the list.

CHAPTER ONE:

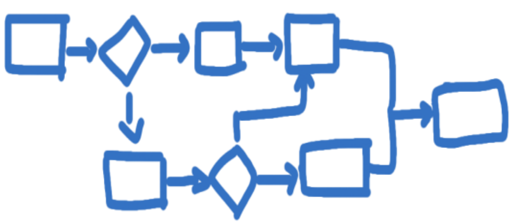
THE PROBATE AVOIDANCE TRUST

The Probate Avoidance Trust is the most often utilized Trust, and is the foundation of any efficient estate plan. It is also a good Trust to discuss in order to build your foundational knowledge of what Trusts are ultimately designed to do.

So lets address the elephant in the room. What is probate? And why do you want to avoid probate?

Probate is the Latin word for "prove". In practical terms, probate, is the proving of your Last Will and Testament before the clerk of the court in the county in which you lived at the time of your death, and then…and here's the part we desperately want to avoid- the administration of your estate through the court system.

My aim here isn't to delve into the ins-and-outs of the probate process, so I won't bore you with all those details. But, for now, understand that the administration of your estate through the court via probate requires various court proceedings for your Executor, the person you name to execute your Will, to qualify, record and make public your Will, file notices, inventories and accountings before the county commissioner of accounts, hold debts and demand hearings, etc.



On average, your Executor, on the heels of your death, is doing the last thing they'd want to be doing. They are spending two years in court, hearings, and accountant's offices, essentially litigating the passage of your assets. All of this can be extremely costly, often to the tune of tens of thousands of dollars drained from your estate. Meanwhile, for these years of probate limbo, your assets aren't being properly invested or, more importantly, utilized for the benefit of your beneficiaries.

Shameless plug time: For a more in depth dive into the considerations surrounding whether to use a Will or a Trust in your estate plan, please check out my book, "*Will vs. Trust*", which is available on Amazon or download from my law firm's website: www.kidwellkent.com.

The core purpose of any properly formulated estate plan is the efficient transfer of your assets. A probate avoidance trust is often the best way to do so for anyone who has a minor child or grandchildren as beneficiaries.

If you own real estate, especially if you own a vacation or investment home in a state other than your primary residence, a probate avoidance trust is often advisable, so as to avoid probate, not only in your home state, but also in the state where the other real estate is located. This second probate is commonly referred to as ancillary administration. And yes, start adding to the the probate fees.

If you own an interest in a business, such as an LLC, a probate avoidance trust is also advantageous to grant your Successor Trustee the right to continue the ongoing concern of the business to wind it down or otherwise carry it on and transfer it to the benefit of a beneficiary.

A probate avoidance trust can be formed either as a Single Grantor Trust or Husband and Wife, as both Grantors and Trustees, and with the Trust becoming irrevocable at the death of the irst spouse.

The Trust, reading as a contract, will state something to the following effect:

"…..upon the death of both Grantors (husband and wife), the rest residue and remainder of the Trust, together with all interest and income accumulated thereon, shall pass equally unto our children, (insert names). In the event that at the time of our deaths, a child has not attained the age of twenty-five (25) years, then their share shall be held by Aunt Susie, as Successor Trustee, in Trust as follows…"

Reads very much like a Will, doesn't it? That's because a Trust, much like a Will, is a testamentary document; to-wit: a document where you say, "when I die, my assets go to blah, blah, blah…"

Here's the key. A Trust, any type of Trust, is just a stack of papers eloquently written by an attorney such as myself. It is an ethereal entity. It is nothing. A Trust can state all live long day where your assets are to go upon the event of your incapacity or death, but it doesn't matter unless the Trust owns those assets. In common parlance, we say that you must fund the trust.

Remember back to the bucket analogy. A trust is a bucket.

We have to pour your assets into the bucket. This funds the trust with your financial assets, real estate, and personal property. Unless you fund the trust, your trust is a worthless stack of papers.

But, if you do fund a Trust, and the Trust controls where your assets go upon your death, you have successfully avoided probate as well as the costs and time-drains associated with the administration of your estate through the court system.

CHAPTER TWO:

MARITAL DEDUCTION TRUSTS

The next type of Trust that is commonly helpful to many of my clients is the Marital Deduction Trust. The Marital Deduction Trust is the Trust that, frankly, confuses the heck out of people when they decide to google trusts after being inspired by someone like Suze Ormon on television.

There are a ton of terms that are thrown around with Marital Deduction Trusts and that's because there are a few different types. There is the QTIP and QDOT, the A-B Trust, the Family Remainder Trust, Marital Perpetuity Trust, Credit Shelter Trust…

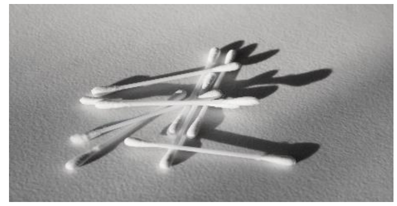
The most often used Marital Deduction Trust is the QTIP. QTIP is short for "Qualified Terminable Interest Property." A QTIP trust is often used in order to take advantage of the marital deduction and still control the ultimate distribution of the assets at the death of the surviving spouse. In short, the goal is double the estate tax deduction, currently $11.18 million dollars. This is done by splitting the estate into two trusts at the death of the first spouse. These two remaining split-off trusts are referred to as the A-B Trusts. Hence the name, A-B Trust, is synonymous with QTIP Trust and Marital Deduction Trust. They are the same thing.

The key in a QTIP is that the terminable interest in the property poured into the trust bucket, such as financial assets and real estate, does not end with the surviving spouse, but instead terminates with other beneficiaries, usually children, grandchildren, or a charity. The advantage to this is that the amount that terminates with the other beneficiaries is not counted in the estate assets of the surviving spouse. The result is that both spouses can utilize their personal estate tax exemption.

It is important to note that a QTIP Trust DOES NOT shelter assets from creditors, or offer medical protection against invasion for the purpose of paying the long term costs of nursing homes, i.e. Medicaid. There are other Trusts that are specifically designed for those purposes, which can be appropriate for some, but the tradeoff, by dint of their irrevocability, is a loss of oversight and control of your assets. These Trusts are discussed later.

Remember that an A-B trust is a joint trust created by a married couple for the purpose of minimizing estate taxes. An A-B trust is a trust that divides into two upon the death of the first spouse. At the death of the first spouse the trust becomes irrevocable and the income from the assets held in the trust, plus an ascertainable standard of principal, are designated to go to the surviving spouse.

QTIP ELECTION = A PECUNIARY OR FRACTIONAL FORMULA MUST BE USED TO DIFFERENTIATE BETWEEN THE MARTIAL OR "A" SECTION, AND THE RESIDUARY, OR "B" SECTION OF THE TRUST.



Trust A accumulates for the benefit of the surviving spouse and income and principal must be available to the surviving spouse.

The B portion of the Trust, frequently called the residuary portion or Family Trust, provides income to the surviving spouse based on a need for "health, support, and maintenance", and the remainder goes to children, or other designated beneficiaries, as the qualified terminable interest.

- ✓ **TAX IMPLICATION: Since the spouse does not have a terminable remainder interest in the "B" Trust/Family Remainder Trust, it is not considered part of the surviving spouse's estate for taxes.**

Note that the Tax Cuts and Jobs Act of 2017, as well as preceding legislation, has made the Marital Deduction variety of the QTIP or A-B Trust less necessary for many Americans. Specifically, since the Federal Individual Estate Tax Exemption has risen to $11.18 million dollars, and that the individual exemption is now portable between spouses, a married couple can now pass $22.36 million dollars to anyone not a spouse, such as children, without the imposition of any Federal Estate Tax. As such, most people do not need to create QTIP/Marital Deduction Trust for the avoidance of estate taxes anymore.

In 2001, before the Bush Era Tax Cuts, the Federal Individual Estate Tax Exemption was $600,000, and was not portable between spouses. QTIP Trusts were a lot more prevalent back then than they are today, as mitigating against the imposition of estate taxes was crucial with the exemption amount being so much lower.

However, there is a Marital Deduciton Trust that is very important for married couples where one of the spouses are not American citizens. This particular type of QTIP/Marital Deduction A-B Trust, is called a QDOT, or Qualified Domestic Trust.

A Qualified Domestic Trust is designed as a marital Trust for the benefit of the Grantor's resident alien spouse. A QDOT allows taxpayers who are not U.S. citizens to claim the marital deduction for estate tax purposes. A QDOT, then, is said to preserve the unified credit between married spouses. This means that collectively, a married couple can leave $22.36 million to their beneficiaries, with no estate tax. Without a QDOT, a married couple with at least one spouse being a resident alien, could only leave $11.18 million free of the estate tax.

Some of the key attributes of a Qualified Domestic Trust are as follows:

- ✓ Marital Trust
- ✓ For the benefit of Grantor's Resident Alien Spouse
- ✓ QDOT= A type of trust that allows taxpayers who are not U.S. citizens to claim the marital deduction for estate-tax purposes. Spouses without citizenship are not eligible for the marital deduction without a qualifying domestic trust.
- ✓ Remainder to children or other beneficiary
- ✓ At least one trustee must be a US Citizen
- ✓ The Trust must provide that that no distribution of principal can be made to the surviving alien spouse unless the trustee has the right to withhold the estate tax on such distributions
- ✓ Assets must be based in US
- ✓ QDOT preserves the unified transfer credit between married spouses

For anyone who is married to someone who is not a U.S. citizen, or anticipates marriage to an alien spouse, a Qualified Domestic Trust is often advisable. A QDOT is essentially a substitute for a Marital Deduction Trust or QTIP Trust when the surviving spouse is not a U.S. citizen.

Generally, the QDOT provides the surviving spouse with all income from the trust assets and even permits certain distributions of principal in the case of defined hardship.

There is one notable exception to the QDOT as a means to circumvent the IRC Section 2056(d)(5) rule that disallows the unlimited marital deduction to non-citizen surviving spouses. In the event the surviving spouse becomes a United States citizen within 9 months of their spouses' death and has been a resident continuously since the date of the spouses' death, the unlimited marital deduction is generally allowed.

Otherwise, a QDOT is essential to many estate plans where one of the spouses is not a U.S. citizen.

CHAPTER THREE:

THE IRREVOCABLE LIFE INSURANCE TRUST

The Irrevocable Life Insurance Trust (ILIT) is a Trust designed to remove life insurance death benefits from the estate of a deceased, insured individual. Individuals who have an estate value near, at, or above the individual estate tax exemption amount (currently $11.18 million in 2018), will purchase life insurance and place it inside this Irrevocable Trust, removing incidents of ownership from themselves, so that the IRS will not count the death benefit from the policy as part of their estate. The life insurance proceeds can then be utilized to pay costs of the funeral, as well as to benefit children, or to leave a legacy, without the hefty estate tax rearing its ugly head. Further, in estates where there is going to be an estate tax, the death benefit from the life insurance policy held in an ILIT can be utilized to pay the estate tax.

The ILIT is also often referred to as the "Crummey Trust". The ILIT was termed a such after a 1968 decision by the Ninth Circuit Court of Appeals, *Crummey v. Commissioner*, 397 F.2d 82 (9th Cir. 1968). In this case, the Ninth Circuit was grappling with the question of whether a gift to a trust, rather than an outright gift to an individual, qualified as a gift for gift tax exemption purposes.

Pursuant to the law, a gift qualifies for the annual gift tax exclusion ($15,000 for 2018) only if the transfer is of a present interest in the property. A present interest is defined as an unrestricted right to the immediate use, possession, or enjoyment of the property or the income from it.

In Letter Ruling 199912016, the IRS considered four factors in determining whether a beneficiary's withdrawal (*Crummey*) right qualified gifts to a trust as present interest gifts:

1. **The trust is required to give the beneficiary reasonable notice in which to exercise the withdrawal right;**
2. **The beneficiary is given adequate time following notice in which to exercise the withdrawal right;**
3. **Upon exercising the withdrawal right, the beneficiary will have the immediate and unrestricted right to an amount equal to the amount contributed to the trust; and**

4. There is no understanding or agreement, expressed or implied, that the withdrawal will not be exercised.

In the typical ILIT/*Crummey* Trust, a periodic contribution of assets, usually in the form of premiums on a first-to-die or second-to-die life insurance policy, is gifted into the trust, accompanied by an immediate withdrawal power that gives the beneficiary the right to withdraw the contribution for a limited time. However, the expectation of the donor is that the power to withdraw will not be exercised. The beneficiary's limited withdrawal right, known as their Crummey Power, renders the gift to the trust a gift of a present interest that can be sheltered by the annual gift tax exclusion.

The trust's beneficiary must be given actual notice of the withdrawal right along with a reasonable period to exercise it, usually 30 days. This notice takes the form of what is commonly referred to as a Crummey Letter, which is sent the beneficiary. The IRS has privately ruled that without a current notice that a gift is being transferred to the trust, it is not possible for a donee to have the real and immediate benefit of the gift. As a result, many ILIT's are drafted to limit the beneficiaries' withdrawal right to the amount of the annual gift tax exclusion or the fair market value of the property contributed to the trust, whichever is less.

Common features of an ILIT:

- ✓ **Remainder to children**
- ✓ **Can draft as a PERPETUITY TRUST so remainder goes to charity.**
- ✓ **Removes the life insurance proceeds from the Grantor/Insured Individual's Estate by irrevocably transferring "incidents of ownership" to the ILIT.**
- ✓ **It is often said that an ILIT is "A PRESENT GIFT OF A FUTURE INTEREST."**
- ✓ **The ILIT must provide that the beneficiaries have a present right to withdraw in the year the gift is made, the lesser of the amount of the gift, or the annual gift tax exclusion ($15,000 currently).**
- ✓ **"Crummey Letter" Notices are Sent 30 days before premium for ILIT Insurance Policy are due.**
- ✓ **The Trustee (CAN'T BE THE GRANTOR) is the owner of the life insurance policy on the Grantor's life.**
- ✓ **Grantor makes a gift each year to the trust of an amount of money necessary to pay the premiums on the insurance and trustee fees.**
- ✓ **Upon lapse of the right to withdraw the gift is made, the trustee pays the premiums on the life insurance policy.**
- ✓ **It is important that the Grantor's spouse ALSO NOT BE TRUSTEE as this may cause the policy death benefit to be included in the surviving spouse's estate.**

CHAPTER FOUR:

THE SPECIAL NEEDS TRUST

A Special Needs Trust is an extremely important estate planning tool when a parent, grandparent or guardian needs to protect assets they would ordinarily leave directly to their disabled and dependent beneficiary, and they wish to preserve the ability to establish Medicaid or other state medical assistance for that disabled dependent.

Medicaid and other state medical assistance programs have very strict guidelines on income and assets an applicant for benefits is allowed to have. Unfortunately, with the costs of medical care skyrocketing, the amount of coverage provided by these programs often leaves a lot to be desired. Think of it this way: there is perhaps enough coverage for medical costs, but there isn't any coverage for standard of living.

Parents with disabled children often want to be able to provide for a higher standard of living than a nursing home for their disabled child, and heaven forbid, they might even want them to enjoy an ice cream cone every once in a while.

However, these simple "comfort" costs can become impractical and downright impossible sometimes when faced with seeking state assistance for medical costs associated with a disabled dependent. A Special Needs Trust affords parents or guardians of a disabled dependent the ability to provide for their loved one's comforts and a standard of living beyond the narrow scope of state income and asset guidelines without disqualifying them from that very state assistance.

In order to qualify as a Special Needs Trust, the Trust must meet all of the following requirements:

- ✓ **The Trust contains assets of an applicant/recipient under 65.**
- ✓ **The applicant/recipient is disabled as defined by the Social Security Act.**
- ✓ **The Trust must be established for the benefit of the applicant/recipient by a parent or guardian, or a court.**
- ✓ **The Trust must require that on the death of the applicant/recipient, the state will receive all amounts remaining in the Trust up to an amount equal to the**

total amount of Medicaid paid on behalf of the applicant/recipient. (If a self-settled SNT)

Disability is defined more succinctly in 42 U.S.C.A. Section 1382c(a)(3)(A)-(D), but generally considers an individual to be disabled if they are:

- ✓ Unable to engage in substantial gainful employment by reason of any medically determinable physical or mental impairment which can be expected to result in death or last for longer than 12 months.
- ✓ Under the age of 18 and has a physical or mental impairment which results in severe and marked functional limitations which can be expected to result in death or which has lasted or can be expected to last longer than 12 months.

Note further that a physical or mental impairment is an impairment that results from anatomical, physiological or psychological abnormalities which are demonstratable by medically acceptable clinical and laboratory diagnostic techniques.

ALERT: Special Needs Trusts are often confused with the similarly named Supplemental Needs Trust.

What is the difference? There really isn't any difference, but there is slightly more to it than that:

Historically, all Special Needs Trusts were called Supplemental Needs Trusts. The name, Supplemental Needs Trust came from the purpose of the Trust itself, which is to supplement the assistance provided by Medicaid, Medicare, Social Security, Supplemental Security Income and other public benefit programs whose level of support is often inadequate.

But, with the 1993 Omnibus Budged Reconciliation Act ("OBRA") authorizing the creation of self-settled trusts under 42 USC 1396p(d)(4)(A), many attorneys called for distinguishing between these new first-party trusts and third-party trusts often created by a parent or guardian. The push was to call self-settled trusts special needs trusts and continuing to call the traditional third-party trusts supplemental needs trusts.

Despite this attorney push, what really happened? Over time the term "supplemental needs trust" has fallen away. The term "special needs trust" refers to the purpose of the trust -- to pay for the beneficiary's unique or special needs. Therefore all supplemental needs trusts are, by nature, also special needs trusts. In short, the name is now more focused more on the beneficiary, while the name "supplemental needs trust" addresses the shortfalls of our public benefits programs.

Special Needs Trust/Supplemental Needs planning is a very good example of where simply googling a few definitions will result in you being more confused than when you began. The terminology is so intertwined it is hardly discernable to even the most acute legal mind.

Special needs trusts now encompass both traditional third-party trusts and first-party trusts created under OBRA, which are often known as (d)(4)(A) trusts, or self-settled trusts. That being said, if you were to map Supplemental Needs Trust to a particular type of Special Needs Trust, it would be to the traditional, Third-Party Special Needs Trust.

The most important difference between third-party Special Needs Trusts and first-party Special Needs Trusts is what happens to the property when the beneficiary dies. Upon the beneficiary's death, the third-party Special Needs Trust (Supplemental Needs Trust) is not required to use the remaining assets to reimburse the state for Medicaid or other benefits received.

Therefore, the third-party Special Needs Trust, or Supplemental Needs Trust, is a useful estate planning tool for those who desire to set aside assets for a disabled beneficiary, preserve essential public benefits for the beneficiary, and control where all of the remaining Trust assets will go upon the beneficiary's death.

But, with third-party Special Needs Trust not requiring payback to the state for benefits received, why would anyone ever set up a first-party Special Needs Trust where benefits are required to be paid back, albeit delayed to after the death of the beneficiary? Given the choice, they wouldn't. First-party Special Needs Trusts are most often created when a disabled individual inherits money or property outright, receives a court settlement, and also when a person who owns assets in his or her name later becomes disabled and now must qualify for public benefits that have an income or asset limitation.

Unfortunately, there are many families across our country that have a disabled child or dependent. A Special Needs Trust can be a very effective tool to provide comfort and a higher standard of living for your loved ones while you are alive, and to leave a legacy that provides for their benefit after you die, without disqualifying them for much needed state assistance, such as Medicaid.

Let's look at an example of a Special Needs Trust being used:

Imagine you're the parents of 3 and your son, Jeff, has autism, Down's syndrome, cerebral palsy, or other physical or mental handicap as a result of a birth defect or an accident later in life. Up until your son was 18, he was a minor, and you as his natural guardian at law had the right to provide for him and make decisions as to his care, etc. This was all on you.

Now, that your son is 18, he is the age of majority, and you now must petition the court to become appointed Guardian of his person and perhaps Conservator of his estate. This gives you the ability to make decisions on his behalf, and even to apply for state Medicaid assistance for Jeff.

But, with strict guidelines on the miniscule amount of income and assets that your son can hold, how can you provide for his welfare and a higher standard of living now, and certainly after you pass? Answer: A Third-Party Special Needs Trust (aka a Supplemental Needs Trust).

Jeff's parents will create a Third-Party Special Needs Trust now, and fund it with assets (often a managed Investment Account and/or a Life Insurance Policy). The Trust fund will grow throughout Jeff's life, and income and principal, with limitations, can be used for Jeff's benefit to the discretion of the Trustee.

If Jeff's parents die before him, their estate plan can provide for their non-disabled children separately, and the Special Needs Trust can provide that when Jeff passes, any remainder will pass to their other children. Medicaid assistance received by Jeff will not have to be repaid.

CHAPTER FIVE:

THE CHARITABLE REMAINDER TRUST

One of the greatest feelings for many is that feeling that comes with giving to a charity of your choosing. The Charitable Remainder Trust is a phenomenal estate planning tool to leverage assets for many tax advantages and to leave a legacy to virtually any church or charitable organization.

A Charitable Remainder Trust is an Irrevocable Trust for the life of the Grantor or Grantors, or for a term of years not to exceed twenty years. Primarily, there are two types of Charitable Remainder Trusts, dependent upon the form of assets used to fund the trust. These are the Charitable Remainder Unitrust, which is funded with real estate, and the Charitable Remainder Annuity Trust, which is funded through the purchase of an annuity or similar vehicle within the trust.

CHARITABLE REMAINDER UNITRUST (CRUT): 

- ✓ **Irrevocable Trust for the benefit of a charity**
- ✓ **Income to Grantor and Spouse for life, using Real Estate**
- ✓ **Remainder to charity(s).**

CHARITABLE REMAINDER ANNUITY TRUST (CRAT):

- ✓ **Irrevocable Charitable trust for the benefit of charity(s)**
- ✓ **Stated annuity income to Grantor(s) for life**
- ✓ **Remainder to charity**

Whenever someone wishes to give to the community, but receive an income stream from their hard-earned assets, the Charitable Remainder Trust accomplishes just that, as well as provides quite significant tax advantages.

In the instance of someone who has real estate that, when sold, will result in a large capital gains tax, a Donor, as Grantor to a Charitable Remainder Unitrust, can eliminate both estate and present capital gains tax on the sale of the real estate by transferring the real estate into the Trust.

In the instance of someone with non-qualified assets, such as stocks held in a mutual fund or other investment account, with holdings that will result in substantial short or long-term capital gains, a Donor, as Grantor to a Charitable Remainder Annuity Trust can transfer the account to the Trust to purchase an annuity within the Trust. This transfer of the assets into an annuity within the CRAT eliminates estate and present capital gains tax on the sale of the stocks.

To be eligible as a Charitable Remainder Trust, the trust must be irrevocable, naming income beneficiaries (usually the Grantor/Donor) to receive not less than 5%, and not greater than 50% of the Trust asset value, on an annual basis. The value of the remainder interest (the amount to go to charity or charities) must be at least 10% of the initial net fair market value of all property placed into the trust.

If the above criteria are met, no capital gains tax results in the sale of of assets placed in a Charitable Remainder Trust. The trust income paid to the Grantor for life will be taxed at the Grantor/Donor's individual income tax rates. However, another attractive tax incentive for Charitable Remainder Trusts is the fact that taxes on the Donor's income can be offset by a charitable deduction up to the appraised amount of the transfer multiplied by an interpolated life remainder factor, with the option to carry the deduction forward for up to 5 years.

Lastly, because the property in the trust reverts to a charity at the death of the Grantor/Donor, there is not estate tax consequence.

BONUS CHAPTER:

THE MEDICAID TRUST

As the baby boomer generation ages, many Americans are facing the very awesome reality that we are living longer. Concomitantly, however, we are also seeing more and more Americans suffering a long term care event. 79% of women age 65 or older will require an average of 3.7 years of long term nursing care. 58% of men age 65 or older will require an average of 2.2 years of long term nursing care. This tells us two major things: 1. Women live longer than men; and 2: a majority of us will need to find a way to pay for Long Term Care.

In Northern Virginia, where my law firm is located, the average cost of nursing home care is just shy of $10,000 per month. With Americans, on average, spending 3 years in nursing homes, or receiving equivalent care, the math is staggering. The average American will need to be covered for, or plan for paying $360,000.00 in Long Term Care costs. These numbers are exactly why healthcare costs are the number one cause of bankruptcy in American, and why many estates are bled dry with nothing to leave behind for future generations.

One method of asset protection is to procure a Long Term Care Insurance Policy. While there are a plethora of policies out there with all sorts of different bells and whistles to consider, applicants often find that they don't qualify for the strict guidelines with pre-existing conditions or risk factors and that the price of the insurance is exorbitant and/or

the coverage is too little. To put it bluntly, a number of insurance carriers have dropped Long Term Care from their shelves because they mispriced it, calculating based upon their morbidity tables and incorrect assumptions on percentages of policies that would lapse. There are, however, many other alternatives to traditional long term care insurance, to include life insurance chassis

with chronic illness riders, for instance, which should be explored as part of a strategy to insure against the inevitable long term care event.

Placing assets into an Irrevocable Medicaid Asset Protection Trust is potentially another very good strategy, specifically for someone who does not have long term care insurance, can't afford it, or does not have enough coverage.

Medicaid is a wide-ranging, jointly funded state and federal health care program for low-income / low resource persons of all ages, though generally for people age 65 or older and in need of assisted long term care.

The very real problem Medicaid applicants face is the income and asset requirement for qualification. In short, an applicant cannot receive Medicaid payments, aka Government Long Term Care, unless assets are spent down to essentially nothing, and there is negligible income. Medicaid is actually administered by the states and in every state, an individual applicant for Medicaid long-term care assistance may have no more than a small amount in "countable resources" in his or her name in order to be "resource eligible" for Medicaid. In Virginia, this Individual Resource Allowance is $2,000.

In addition to the resource eligibility gate, there is the income eligibility hurdle to overcome in order to qualify for Medicaid. In Virginia, the Department of Medical Assistance Services administers the Medicaid program, and a local Department of Social Services determines eligibility. A Medicaid applicant can qualify in Virginia so long as their income is limited to only $2,250 per month.

Another key factor in asset protection planning is the Medicaid Lookback Period. The Lookback Period for Medicaid is 5 years from the date of application. There can be no uncompensated transfers or gifts within that lookback period, with few exceptions. To the extent any of these have been made, an applicant will be required to pay that amount toward their long term care before Medicaid will begin to cover anything.

All of these strict income and asset eligibility requirements for Medicaid require a massive spend down of one's assets. This is not conducive to the married couple where the most important goal is to ensure that the spouse remaining at home is able to live the remaining years of his or her life without having to suffer a drastic reduction in standard of living. For a single or widowed person, the most important goal typically is to be able to enjoy the highest quality of life possible in the event of a long term care scenario, but this goal is hamstrung by Medicaid's very strict eligibility thresholds.

Assets that are protected through proper estate planning, however, can be used to provide a nursing home resident with an enhanced level of care and a better quality of life while in a nursing home and receiving Medicaid benefits. Trust funds can be used to hire a private nurse or health aide to provide assistance beyond the base levels covered under Medicaid

and can also be used to purchase things such as special medical devices, upgraded services, and trips to the barber shop.

Finally, with proper asset protection planning, one can still leave a financial legacy for their beneficiaries, without being required to spend down all their assets.

A properly drafted Medicaid Asset Protection Trust will:

- ✓ **be protected for Medicaid purposes (completely after five years, with partial protection possible in less than five years).**
- ✓ **Trust assets can be used to enhance quality of life beyond Medicaid's low standard of living.**
- ✓ **Assets the remain in the Trust after you pass will transfer to your beneficiaries, free of Medicaid payback.**
- ✓ **Trust provides you all ordinary income from the trust financial assets and the right to use any trust-owned realty or tangible personal property.**

Let's look at an example of a Medicaid Asset Protection Trust in action:

Kristin, at 75, is relatively healthy and self-sufficient. But, she's not getting around as well, and is worried about the costs of long term care, especially since she's not insured in the slightest. Kristin meets with an experienced elder law and estate planning attorney who drafts a Medicaid Asset Protect Trust, into which Kristin transfers her home which is worth about $400,000. Kristin decides that she will keep her $135,000 IRA, which is her only other significant asset, out of the trust.

For the next four years, Kristin remains relatively healthy, and is able to live on her $1,500 per month retirement income plus required minimum distributions from her IRA. Then, one morning, on her way to the mailbox, Kristin trips and takes a hard fall, breaking her leg. After three days in the hospital and weeks of rehab, it's clear she needs long term nursing care.

At this point, Kristin has only $120,000 in her IRA, which will pay for less than 6 months of nursing home care. At this point Kristin will need to spend down her IRA to $2,000. But, in the meantime, the Trustee of Kristin's Medicaid Asset Protection Trust can sell Kristin's house, payoff any outstanding mortgage, and then deposit the proceeds back into the Trust. Once the IRA moneys are spent down to $2,000 and it has been 5 years from the date of the making of the Trust, the proceeds from the sale of the $400,000 house can be used for Kristin's benefit as a supplement to Medicaid.

FINAL THOUGHTS:

The advice given in this book is not meant to serve as legal advice and should not be relied upon without consideration of your own fact pattern. All estates should be scrutinized individually, and no estate planning practitioner should approach a client with a cookie-cutter approach to an estate. I advise that everyone seek legal counsel when planning for their estate.

In this age of the internet, it is very easy to get lost in the world of google searches. You will find that there are countless different types of trusts, with different names and purposes, and your head may spin. It is very easy to get lost and think you understand a core estate planning principle regarding a particular type of Trust when in fact, you are misguided or misinformed altogether.

My thought is this: you have worked tirelessly throughout your entire life to build up your financial wealth. Why try and save a few hundred dollars and prepare a will or trust from an internet form and risk, literally, all that you have gained, to taxes, and legal proceedings? And in particular regards to Trusts, certain codified, specific and very detailed language must be present for the Trust to accomplish it's intended purpose, whether it be for asset protection, probate avoidance, or otherwise. Don't risk your assets and your legacy to misinformation and my best advice is to always consult an attorney regarding your estate plan, especially if you think a trust may be beneficial for you.

That being said, it is better to have something in place, rather than nothing. In fact, that is the purpose of a will, as previously discussed. A will is meant to serve as the catch-net for your estate, and make sure that nothing slips through the cracks into the land of intestacy and court appointed administration of your estate.

Lastly, I always joke with my clients: "A Will or Trust can always be amended, because your estate plan is not etched into stone until you are."