

Customize Your Estate Plan with Trusts

By Bonnie J Orr, CPA

Do you think trusts are only for the very wealthy? Do you think trusts are restrictive and expensive? Think again - A trust can be an excellent tool to use for your unique estate planning goals. People are often surprised to learn that a trust can be tailored to address their own special goals, taking into account current tax rules and other factors.

Simply stated, a trust is an arrangement in which legal title to property is held by one or more trustees who manage the property for another's benefit. A trust can be set up to benefit the person who created it (known as the grantor), it can be set up for beneficiaries named by the grantor, or for both.

Trusts can be set up to operate during the grantor's lifetime and beyond, or can be set up to operate pursuant to the grantor's will. A trust set up to operate pursuant to a will does not exist until the will is probated and the trust is funded by the Executor of the estate. You can even include a provision in your will, called a disclaimer, which in effect leaves certain decisions regarding creation of a trust up to your beneficiary. Trusts can be revocable (you can change your mind during your lifetime) or irrevocable.

In short, trusts are very flexible entities that can be tailored to accomplish many purposes. Among other things, trusts can:

1. help you to manage your property and investments more easily and expertly;
2. help you to avoid probate costs;
3. keep life insurance proceeds out of your estate;
4. protect the interests of your minor and adult children;
5. preserve an estate tax break for the amount of the federal unified credit (\$2 million in 2008, \$3.5 million in 2009)
6. allow you to get the estate tax marital deduction for property that ultimately will go to other beneficiaries you name in your will or trust; and
7. let you get an income tax deduction for a contribution to charity while you continue to get income from the contributed property.
8. help you to protect your assets from creditors such as nursing homes and judgment creditors, etc.

The tax consequences are as varied as the uses to which trusts can be put. The creation of a trust for someone else's benefit may be subject to estate or gift tax, but certain trusts can qualify for discounts to the amounts subject to estate and gift tax.

As far as income taxes go, trust income can be taxed to the grantor, the trust, or the beneficiary, depending upon how the trust is set up and what it is intended to do.

Trusts need trustees. Choosing a suitable trustee must take into account the type of trust involved. Sometimes the grantor can serve as a trustee or co-trustee. The trustee could be another family member, a friend, a professional adviser, or a financial institution. The trust can include a provision for the beneficiary to change trustees, within limits or not. It is up to you, as the creator of the trust, to determine how much flexibility you want to give the beneficiary in choosing trustees.

It is up to you, as the creator of the trust, to determine how much flexibility you want to give the trustee in providing distributions to the beneficiary. The trustee could be directed to pay out income only, or a percentage of the value of the trust each year. The trustee could be directed to pay out principle for health, education, maintenance and support, or not. It is up to you, the creator of the trust.

There are trade-offs. The amount of flexibility will determine the estate and income tax consequences. A tax advisor who specializes in estates and trusts will be able to advise you as to how your goals will affect your estate and income tax costs.

Bonnie J Orr, CPA is a partner at Judelson, Giordano and Siegel, CPA, PC. She is a member of the American Institute of Certified Public Accountants and the New York State Society of Certified Public Accounts. Bonnie specializes in the area of estates and trusts.

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