ESTATE PLANNING GUIDE FOR PARENTS

As parents of young children, there are crucial items to consider with respect to your Last Will & Testament. Estate planning is essential for parents of young children for two main reasons. The first is to choose a Guardian to raise your minor children in the event both parents pass away and this person should be named in your documents. The second is to provide for the child financially through a trust because as minors, they cannot legally “inherit” assets directly. Even life insurance proceeds should pass through a trust to a minor child.

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Dying Intestate (without a Will)

Dying intestate (without a will) in NYS means that your spouse gets the $50k of any assets held in your sole name and the remaining assets are distributed 50% to the spouse and the remainder to the children. This is a problem when you have minor children since they cannot inherit assets. Moreover, this may not be the intent since most people assume assets pass to the surviving spouse. If both parents pass away, the children inherit 100% of the assets.

If a guardian is not nominated by the parent, someone must petition the court to be appointed. This could lead to different family members and friends asserting control, with a judge ultimately deciding who will raise the children. Of course, if one parent dies, the other parent will become the natural guardian unless the surviving parent is challenged as unfit.

If a testementary trust is not set up for the children's benefit, then a "guardian of the property", is appointed by the court to handle the finances. The potential problem with such a scenario is that the child will often inherit all

THE SOLUTION

There is a simple way to avoid the Court choosing who will care for your children using a Last Will & Testament or a Revocable Trust document:

- Appointment of a Guardian.
- Creation of a Testementary Trust.

CHOOSING A GUARDIAN

Choosing who will raise your children in the event you pass away is not an easy task. There is no magic formula for choosing the right guardian. Everyone's situation will be unique and no one factor outweighs another.

1 WILLINGNESS

A discussion on whether a proposed Guardian is willing to take your children can be awkward, but it is better to have the conversation up front rather than having the Guardian turn down the appointment and putting the decision back into the hands of the Court.

2 GEOGRAPHY

If your children are in a certain school and area where they are comfortable, it may be important to keep that consistent. Naming a guardian that lives out of state may make the transition more traumatic for the children. If the proposed guardian lives out of the country, an alternate or standby guardian should also be named to take temporary custody of the children.

3 AGE

Consider the age and health of the Guardian. Many young couples initially think of their parents. This may be the appropriate answer for your family, but make sure that their age and potential retirement plans do not conflict with the raising of small children.

4 FAMILY SITUATION

Some parents may prefer their child to grow up with other children their own age, while others find value in a smaller family unit. If the proposed guardian already has many children, he or she may not have the money or energy to devote to more. Is the house big enough? A single person may not have the resources to work and raise small children – but would they be willing to relocate to your home?

5 SHARED VALUES

You should consider the Guardian's values– are they the same values that are important to you? Religion, politics, and moral beliefs are important to consider because they will likely mold how a child develops.

Leaving Assets to Minors

Since anyone under 18 years old cannot legally receive assets, a testamentary trust must be set up in your Will or Revocable Trust to receive those assets and a Trustee appointed. A “Testamentary” trust simply means that it is created upon your death. This type of trust is usually only “triggered” upon your death, and if married, the death of your spouse. The Trust holds assets for the benefit of your children until they reach a certain age and the assets pass directly to them. The Trustee (who can be the Guardian) will have access to the trust funds to pay for all expenses related to raising your children.

Separate Trusts vs Common Pot Trust

If you have one child and no possibility of having any more, then your estate planning attorney will set up a testamentary trust for that child. If you have more than one child or may possibly have more children, you have the choice of either establishing separate trusts for each child or a Common Pot Trust. A Common Pot Trust is one single trust that holds all of your assets and is to be used by your Trustee for the benefit of all of your children. This type of trust mimics the way we raise children – we never know how much care any particular child may need. When the youngest reaches a certain stated age, at least 18 years old, any remaining assets are divided into separate trusts for each child. Those separate “Descendant’s Trusts” then operate independently, leaving assets to the child when he or she reaches a certain specified age.

Alternatively, the minors’ Common Pot Trust can simply end and any remaining assets left to each child outright. Conceivably a Common Pot Trust could last as long as you wish, with a Trustee continuing to control distributions indefinitely. This is similar to the way many so called dynasty trusts operate – passing wealth down through the generations.

Descendant's Trust

Whether you decide to have a Common Pot Trust turn into a Beneficiary Trust depends on the amount of money you plan to leave, how much control you want to assert, and convenience. Many people with adult children establish Beneficiary Trusts instead of leaving assets to their children outright. This is to either protect the children from themselves and/or creditors and divorce.

If a Common Pot Trust ends when the youngest reaches 18 or 21 years old, many parents believe that is still too young to inherit. Some parents prefer that the Trustee remain in charge of assets until each child reaches a more mature age – or stagger withdrawals at stated ages. For example, 25% at reaching 23 years old, 25% at reaching 27 years old, and perhaps the remaining assets at 35 years old. Although the Trustee can still make disbursements using his or her best judgment, the child is guaranteed a percentage at the age you choose. This is purely a personal choice.

TAX ISSUES

Most trusts are structured so that the beneficiary receives all the income generated from the trust which is then taxed as ordinary income to the beneficiary. This is because trusts pay a high federal income tax rate – more than twice as much a single individual and three times as much as a married couple. Trusts also pay the 3.8% net investment income tax and more in capital gains. An estate planning attorney who can walk you through how to avoid these issues.

The so-called Kiddie Tax would apply to any income generated each year from the trust, unless bnoth parents had passed away. The tax is calculatied at parent's so that it's once again based on the surviving parent's marginal tax rate

Choosing a Trustee

Choosing a Trustee for a child's trust is much different than choosing a trustee of an asset protection trust because the duties are very personal. In estate planning, a Trustee refers to an individual or institution who holds assets on behalf of a beneficiary and distributes assets according to the terms of the trust instrument. Therefore, your Trustee will manage assets for the children and make disbursements in their best interest until they reach a certain age.

1

TRUSTWORTHY

It is difficult to anticipate the future needs of children when drafting the terms of the trust or even what the world will be like at that time. This is why Trustees of such trusts are given broad discretion to make disbursements for the child's needs.

It is always important to discuss with a potential Trustee what is expected. The Trustee will have to carry out the express terms of the trust and must understand how income and principal is to be distributed and at what intervals. Moreover, you should inform the Trustee what you believe is important in raising your child – such as travel or musical instruction—and include such terms in your trust.

2

ORGANIZED

An attorney or tax professional can assist your trustee once a year or so to make sure that the Trustee is keeping accurate accounts. But a Trustee must keep track of funds expended and keep the beneficiaries informed as to their right to income and principal from the trust. The latter is especially important as your child reaches the age of majority and make begin requesting funds from the trust. At the beginning of each year, the Trustee should work with the guardian in designing a draft budget.

3

RESPONSIBLE

The Trustee must be savvy enough to make sound investments or utilize a financial advisor. As a fiduciary, your Trustee has a duty to prudently invest the trust assets and is subject to potential liability for mismanagement. A clause can be included limiting the trustee liability to bad faith, but you certainly do not want to name someone who makes risky investments or refuses to seek out professional advice.

Should the Guardian be the Trustee?

The most likely person to appoint as Trustee is the acting Guardian. This way he or she has ready access to funds needed to raise your children. You have already entrusted your children to this person, so why not their money as well? In many cases this is the logical choice. However, a completely different Trustee could be named to act alone or as a co-trustee with the acting guardian. An independent Trustee may be especially warranted when parents are divorced or the guardian is not financially stable.

Last Step

CHANGING BENEFICIARY FORMS

Most young parents' biggest assets are insurance policies and retirement accounts. Creating testementary trusts to hold assets for children would make little sense if the children ended up inheriting these assets outside the trust we carefully crafted in your Will or Revocable Trust. You must change your beneficiary forms to reflect that your children will inherit these assets in their trusts. If you are married, this is a change to the "contingent" beneficiary because your spouse remains your "primary" beneficiary. If you are unmarried, then the trust created for the benefit of your children becomes the primary beneficiary. Your estate planning attorney will provide this information

Having a comprehensive plan in place gives you peace of mind and if the worst-case scenario does come to pass, an already difficult period will go much smoother and ensure the right person is raising your children.

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