ESTATE PLAN SHOCKERS

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Probate Nightmare

Hypo #1- Brian just inherited his mother's house in Del Mar as a result of his mother's recent death. Although she had the home in her name, she left it to Brian in a testamentary Trust in her Will. The home is valued at $2.5 Million with a $1.5 Million mortgage.

Results: Because the home is left in her will, it must go through the probate process which could take up to 1 ½ years in San Diego County. Probate fees are assessed against the Fair Market Value of $2.5 Million as debt is not allowed to reduce the gross estate value for statutory Probate fees in California.

Catastrophic Catastrophe

Hypo #2- Carole and Ben have been in a second marriage for 10 years. They each have separate property in their own names and a community property home valued at $600,000. Carole's separate property estate is valued at $500,000 and Ben's is valued at $200,000. Prior to marriage, they entered into a Pre-Nuptial Agreement to protect their separate property rights. Neither have long term care insurance.

Ben, age 65, has a major stroke which will require years of care in a skilled nursing facility. The couple is now subject to the catastrophic health laws in California and the Deficit Reduction Act, a new catastrophic health law in California.

Results: Under the new Deficit Reduction Act, DEFRA, the couple are assigned proportional amounts of the estate. DEFRA in following the previous federal law MCCA, supersedes California's community and separate property laws. As a result, Carole is assigned the Community Spouse Resource Allowance this year in California of $109,560 of separate property, countable assets. Ben is assigned the balance of the separate property, countable assets of $591,440 which must be spent down before he is eligible for Medi-Cal. Again the separate property rights of Carole and the Pre-Nuptial are ignored by this law and her separate property estate is vulnerable to spend-down for Ben's care.

IRA Tax Trap

Hypo #3- Steve designates his son, David, as beneficiary of his $2 Million IRA. Steve creates a Living Trust in which he transfers his home, valued at $400,000, and other non-retirement accounts, valued at $150,000, and signs Powers of Attorney created by a Trust Mill. David is the beneficiary of his father's entire estate and intends that the IRA be utilized for continued growth and his retirement.

Steve loses capacity at age 70 and David realizes that his dad must begin to take distributions at the age of 70 ½ from the IRA. At age 75, Steve dies and David goes to the bank and rolls the IRA into his name which is now valued at $2.2 Million.

Results: Since Steve arranged his estate plan with a Trust Mill, his Power of Attorney did not include IRA provisions. Also, because the Trust could not own the IRA, David, as Successor Trustee, had no authority over the IRA. As a result, the IRA custodian, Schwab, demanded that David obtain a Court order through a Conservatorship to initiate the Minimum Required Distributions for Steve beginning at age 70 ½. In order to avoid a 50% penalty for failure to distribute, David had to obtain temporary orders then permanent orders and account to the Court for the five years the Conservatorship was open. Altogether, the Court proceedings, attorney fees, CPA fees and costs were about $18,000.

After David rolled the IRA into his name, Schwab issued a 1099 indicating a distribution of the IRA fund in the year of Steve's death which terminated the growth and tax deferral and caused a taxable event on the entire $2.2 Million IRA.

Hidden Trust Powers

Hypo #4- Joe and Janice enter a second marriage with a blended family. Joe has 2 sons by a prior marriage and Janice has 2 daughters. They create an A-B Trust with their $3 Million joint estate in which each child is to receive an equal share of the estate on the death of the surviving spouse. The Trust includes a General Power of Appointment under the Survivor's Trust and Portability provisions for Federal Estate Tax. On Joe's death, Janice as the surviving Trustee splits the estate valued at $3 Million in equal shares of $1.5 Million each between the Decedent's Trust B and the Survivor's Trust A. She also elects Portability of Joe's remaining exemption.

During the 10 year remainder of her life, Janice uses the Decedent's Trust B for her health, maintenance, and support. On Janice's death, the Decedent's Trust is valued at $600,000 and the Survivor's Trust is valued at $1.2 Million. Before her death, Janice exercised the General Power of Appointment in her Survivor's Trust which was effective on her death to appoint the entire Trust A in equal shares to her daughters.

Results: After the death of both spouses, the A and B Trusts are to be combined and divided into 4 equal shares for the children. There is $600,00 remaining in Trust B and zero in Trust A for a total of $600,000. Thus, each child receives a distribution of $150,000. However, the 2 daughters were appointed the Survivor's Trust A equally and each received $600,000 from that Trust. As a result of the exercise of Powers of Appointment, each daughter received $750,000 and each son $150,000 of the estate. This clearly was not what the spouses agreed upon when they initially created the Trust.

Proper Estate Planning can provide solutions to all of the foregoing problems.

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