

THE C & D NEWSLETTER



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Published by:
RICHARD K. CITRON
DAVID R. DEUTSCH
MICHELLE LeCOLST-JOHNSTON
Attorneys

WILLS AND TRUSTS

Wills

A will is a written instrument by which a person disposes of property at death. A will is always subject to change during the person's lifetime. It conveys no present interest in property until the person's death. In California there are three types of wills: (a) a "holographic" or handwritten will; (b) a statutory will; and (c) a formal will, prepared by an attorney.

Holographic Will. A holographic will is a will where the signature and all material provisions are in the handwriting of the person making the will. It is not necessary for a holographic will to be witnessed in order to be valid. One major problem with a holographic will is the possibility of ambiguous language. For example, if the will provides that "I give \$30,000 to my three sons," does the will mean that all three sons are to divide the \$30,000, or that each son is to receive \$30,000? Or, if the will provides that "I leave all the money in my account at City National Bank," does this mean all the money in the account when the will was made, or when the person died? Another ambiguity arises if the person had two accounts at City National Bank. A second problem with a holographic will is that a person may unintentionally fail to provide for a person and thus disinherit that person. For example, if a person leaves all his property "to my only son, or, if the son is not living at the time of my death, to my son's children," the person will have disinherited his son's wife, who will then have to raise the children under the restrictions of a court supervised guardianship (which would also add to probate expenses). Often, a self drafted will does not designate successor trustees, or comply with technical requirements for establishing trusts. If a person makes grants of specific amounts of money to certain friends, there may be very little left for the real object of his bounty due to an unanticipated reduction in the estate or failure to account for liabilities.

Statutory Will. California has a statutory will form. This form is designed for simple situations, and may not be changed in any manner. As an example, the statutory will with trust distributes all of the property to the children when the youngest is twenty-one. It is not designed to reduce estate taxes or any other taxes.

Formal Will. A formal will prepared by an attorney is the most common type of will in California. A formal will generally contains the following provisions: (a) the testator's marital status, and names of his spouse and children; (b) the name of the person (called the executor) designated to carry out the instructions of the will, pay debts and taxes and manage the property until it can be delivered to the beneficiaries; (c) provisions for payment of debts and taxes; (d) provisions setting forth to whom and in what manner the testator's property is to be disposed; (e) provisions for alternate dispositions of property if the original disposition becomes impossible for any reason, such as the death of the original beneficiary; (f) provisions for disposition of property in the event of the simultaneous death of the husband and wife; (g) provisions for the guardianship of minor children; and (h) provisions for trusts, (for example a provision that certain property is to pass in trust to the testator's children for life, with the remainder given outright to their grandchildren. A formal will must be signed before at least two witnesses. If the person is not of sound mind or is acting under undue influence when the will is signed, it is invalid. Thus, it is advisable to have the attorney supervise the making and execution of the will. A properly drawn will may simplify and reduce the cost of the probate proceedings.

Dying Without a Will. If you die in California without a will, California's laws of succession determine who shall inherit your property and in what proportions your property shall be distributed. The law is inflexible and does not take into account the particular circumstances or needs of your heirs, or you desires. For example, if a father owning only community property dies without a will, his wife inherits everything and his children inherit nothing. Where the decedent leaves minor children, a guardian will have to be appointed to administer the minor's property. The guardian is subject to court supervision as to the type of investments and expenditures he can make. The court will also appoint an administrator (who may not be the surviving spouse or a member of the decedant's family) to locate the decedent's property, collect all debts due the estate, pay all debts and taxes and distribute what is left according to the laws of succession.

Probate

Probate proceedings are court proceedings which determine whether the deceased person left a valid will and whether the will should be admitted to probate. In probate proceedings, the court appoints a personal representative for the estate. The personal representative is known as the "executor" if specifically named in the will, as the "administrator with will annexed" if

not named in the will, and as the "administrator" if the decedent left no valid will. The representative (a) inventories and collects the assets of the decedent, (b) pays valid creditor's claims, federal and state taxes, and probate referee fees, attorney's fees and fees of the representative (which are set by law), and (c) distributes any remaining assets to the heirs. The representative is authorized to sell the decedent's assets in order to pay the decedent's debts. The time involved in probating a will depends on the nature and complexity of the estate. If there are few assets and claims, the probate may be concluded within six months; however, if there are substantial assets which require valuation for tax and probate purposes, such as jewelry, antiques, real estate or closely held stock, the probate proceedings can last much longer. Having a will probated often takes over a year in these situations, and probate proceedings have been known to drag on for several years in complicated estates.

Trusts

In general, trusts permit the owner of property to provide for the management and disposition of property. Basically, there are three types of trusts: (a) the revocable living trust; (b) the irrevocable trust and (c) the testamentary trust.

The Revocable Living Trust. Generally, in a revocable living trust, an owner ("grantor") transfers property to himself as trustee to be managed for his own benefit (beneficiary). A revocable living trust (also called an inter vivos trust) may be canceled or changed during its existence. The trust agreement provides that the trustee is to pay the grantor all of the income from the trust during his lifetime, together with such amounts of principal as desired at any time. After the grantor's death, the trust assets automatically pass to the grantor's heirs. The grantor may change the assets in the trust, the successor trustee, or the terms and beneficiaries of the trust at any time. Upon the death of the grantor, the trust becomes irrevocable.

The advantages of a living trust include the following: (a) the costs and delays of probate are avoided; (b) if you become unable to care for yourself due to mental or physical disability, the successor trustee may assume management of the trust, thus avoiding the costs and publicity of a court conservatorship proceeding; and (c) privacy, since the contents of the trust are not a public record as is the case with a probate will. In addition, a living trust can provide a mechanism for professional management of your assets, if you are too ill or not interested in managing them yourself.

The disadvantages of a living trust include (a) the cost and effort involved in transferring all of your assets to the trust; (b) the cost and expenses of setting up the trust; and (c) the cost and expense of administering the trust if you name a trustee other than yourself. Transferring property to a living trust has no impact on property taxes or income taxes, and a separate tax return for the living trust is not required. Thus, establishing a living trust does not reduce estate or income taxes.

Irrevocable Trust. An irrevocable trust is created during your lifetime. Certain assets are transferred in for the benefit of heirs. Those assets transferred in may be permanently removed from the estate of the transfer or if they qualify as part of the available exclusions from estate taxes, which are \$10,000 per year per donor, plus \$600,000 one time lifetime per donor.

The benefit of such transfer is that further appreciation is removed from the estate of the donor, as well as current earnings on these funds are taxed to the beneficiaries (except that children under 14 are taxed at their parents rate on earnings over \$1,000 per year). The disadvantages of an irrevocable trust are that once given, the gifts cannot be taken back, and the trustee generally must be someone independent of the donor, who will then control the assets pursuant to the terms of the Trust.

Testamentary Trust. A testamentary trust is created by a will and takes effect upon the grantor's death. If the trust is properly prepared, it will remove some of the property from the grantor's gross estate and thus may result in significant tax savings. Some of the more common testamentary trusts are the "bypass trust", which avoids estate taxes resulting from the bunching of property in a single generation; the "marital deduction trust", which defers estate tax until the surviving spouse's death; the "widow's election trust", used in situations in which the spouses disagree as to who is to receive their property; and the "sprinkling trust" in which an independent trustee is given broad discretion to accumulate or distribute, (or "sprinkle"), income among various beneficiaries so as to incur the least amount of income tax to the trust's beneficiaries. These estate planning devices may also be incorporated in a living trust or will.

Summary

Wills and trust permit you to determine who will administer your estate, who will be the guardians of minor children, and who will receive your property. If properly structured, a will or trust may result in significant tax savings. There is no general form that is best for everyone; rather each person should analyze their particular situation and determine whether a will or trust, or both, fits their special needs.

This complimentary newsletter is intended to provide general information. Because of the complexities and constant changes in the law, it is important to seek professional advice before acting on any of the matters covered herein.

