Trusts 101

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Trusts 101

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Where to Begin?- An Overview of Trusts

Submitted by John H. Killeen

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WHERE TO BEGIN? AN OVERVIEW OF TRUSTS

I. What is a trust and what are the key terms?

The creator of a trust is called the "Settlor," and the people for whom the trust is created to benefit are called the "Beneficiaries." The "Trustee" is the person appointed to administer the trust, and is entrusted to do so based upon fiduciary duties owed to the beneficiaries. This means that a Trustee must at all times act in the best interest of the Beneficiaries, and must uphold this responsibility without the slightest appearance of bias or personal interest.

A trust is an arrangement whereby legal title to property is held by the Trustee while the beneficial interests are held by the Beneficiaries. An express trust is controlled by the specific terms of a written trust instrument created by the Settlor and by applicable Georgia law. Wealthy Settlors and their advisors expend a great deal of time and effort to spell out the Settlor's intentions for the distribution of the trust's assets. The goal of a trust is to separate the assets from the beneficiaries and others. This is to protect others from themselves, protect assets from creditors, avoid probate, and to defer taxes and/or creditors.

II. Major Laws Governing Creation and Administration of a Trust

The Revised Georgia Trust Code of 2010 is set forth in O.C.G.A. § 53-12-1, *et seq.*, and contains the major laws governing trusts in the State of Georgia.

O.C.G.A. § 53-12-2 specifically defines the terms relating to trusts as follows:

(1) “Ascertainable standard” means a standard relating to an individual's health, education, support, or maintenance within the meaning of Section 2041(b)(1)(A) or 2514(c)(1) of the federal Internal Revenue Code of 1986.

(2) “Beneficiary” means a person for whose benefit property is held in trust, regardless of the nature of the interest, and includes any beneficiary, whether vested or contingent, born or unborn, ascertained or unascertained.

(3) “Express trust” means a trust as described in Code Section 53-12-20.

(4) “Foreign entity” means:

(A) Any financial institution whose deposits are federally insured which is organized or existing under the laws of any state of the United States, other than Georgia, or any subsidiary of such financial institution;

(B) Any other corporation organized or existing under the laws of any state of the United States, other than Georgia, and chartered or licensed under the laws of such state; and

(C) Any federally chartered financial institution whose deposits are federally insured having its principal place of business in any state of the United States, other than Georgia, or any subsidiary of such financial institution.

(5) “Implied trust” means a resulting trust as described in Code Section 53-12-130 or a constructive trust as described in Code Section 53-12-132.

(6) “Nonresident” means an individual who does not reside in Georgia.

(7) “Person” means an individual, corporation, partnership, association, joint-stock company, business trust, unincorporated organization, limited liability

company, or other legal entity, including any of the foregoing acting as a fiduciary.

(8) “Private foundation” means a private foundation as defined in Section 509 of the federal Internal Revenue Code.

(9) “Property” means any type of property, whether real or personal, tangible or intangible, legal or equitable, and shall include digital assets and electronic communications, as such terms are defined in Code Section 53-13-2.

(10) “Qualified beneficiary” means a living individual or other existing person who, on the date of determination of beneficiary status:

(A) Is a distributee or permissible distributee of trust income or principal;

(B) Would be a distributee or permissible distributee of trust income or principal if the interests of the distributees described in subparagraph (A) of this paragraph terminated on that date without causing the trust to terminate; or

(C) Would be a distributee or permissible distributee of trust income or principal if the trust terminated on that date.

The Attorney General has the rights of a qualified beneficiary with respect to a charitable trust as defined in Code Section 53-12-170, and a person appointed to enforce a trust created for the care of an animal under Code Section 53-12-28 also has the rights of a qualified beneficiary.

(11) “Settlor” means the person who creates the trust, including a testator in the case of a testamentary trust.

(12) “Spendthrift provision” means a provision in a trust instrument that prohibits transfers of a beneficiary's interest in the income or principal or both.

(13) “Trust” means an express trust or an implied trust but shall not include trusts created by statute or the Constitution of Georgia.

(14) “Trust instrument” means the document, including any testamentary instrument, that contains the trust provisions.

(15) “Trust property” means property the legal title to which is held by the trustee. The term also includes choses in action, claims, and contract rights, including a contractual right to receive death benefits as the designated beneficiary under a policy of insurance, contract, employees' trust, or other arrangement.

(16) “Trustee” means the person or persons holding legal title to the property in trust.

O.C.G.A. § 53-12-2.

O.C.G.A. § 53-12-20 sets forth the general requirements for creating an express trust in Georgia, and states as follows:

(a) Except as provided in subsection (d) of this Code section, an express trust shall be created or declared in writing and signed by the settlor or an agent for the settlor acting under a power of attorney containing express authorization.

(b) An express trust shall have, ascertainable with reasonable certainty:

(1) An intention by a settlor to create such trust;

(2) Trust property;

(3) Except for charitable trusts or a trust for care of an animal, a beneficiary who is reasonably ascertainable at the time of the creation of such trust or reasonably ascertainable within the period of the rule against perpetuities;

(4) A trustee; and

(5) Trustee duties specified in writing or provided by law.

(c) The requirement that a trust have a reasonably ascertainable beneficiary shall be satisfied if under the trust instrument the trustee or some other person has the power to select the beneficiaries based on a standard or in the discretion of the trustee or other person.

(d) In the case of a trust created pursuant to 42 U.S.C. Section 1396p(d)(4)(B) by an agent acting for the settlor, the power of attorney need not contain an express authorization to create or declare a trust.

O.C.G.A. § 53-12-20.

A trust does not require any specific words, as set forth in O.C.G.A. § 53-12-21:

(a) No formal words shall be necessary to create an express trust.

(b) Words otherwise precatory in nature will create a trust only if they are sufficiently imperative to show a settlor's intention to impose enforceable duties on a trustee and if all other elements of an express trust are present.

O.C.G.A. § 53-12-21.

O.C.G.A. § 53-12-23 requires that a Settlor have sufficient capacity to create a trust, and requires as follows:

A person has capacity to create an inter vivos trust to the extent that such person has legal capacity to transfer title to property inter vivos. A person has capacity to create a testamentary trust to the extent that such person has legal capacity to devise or bequeath property by will.

O.C.G.A. § 53-12-23.

Georgia specifically defines testamentary capacity to bequeath property pursuant to a will in O.C.G.A. § 53-4-11 as follows:

> (a) Testamentary capacity exists when the testator has a decided and rational desire as to the disposition of property.
>
> (b) An incapacity to contract may coexist with the capacity to make a will.
>
> (c) An insane individual generally may not make a will except during a lucid interval. A monomaniac may make a will if the will is in no way connected with the monomania. In all such cases, it must appear that the will expresses the wishes of the testator unbiased by the insanity or monomania with which the testator is affected.
>
> (d) Neither advancing age nor weakness of intellect nor eccentricity of habit or thought is inconsistent with the capacity to make a will.

O.C.G.A. § 53-4-11. Pursuant to Georgia case law interpreting O.C.G.A. § 53-4-11, a testator possesses the capacity to make a will if, at the time of executing it, the person understands that a will is intended to dispose of their property after their death, is capable of remembering generally what property and persons related to them are subject to the will's disposition, and is capable of setting forth an intelligent scheme to dispose of their property. *Strong v. Holden*, 287 Ga. 482, 483(1), 697 S.E.2d 189 (2010). Evidence of the testatrix's condition both before and after execution of the will is admissible to demonstrate testamentary capacity. *Id*. The mental capacity to make a will is modest, and the law requires only that the testator have a "decided and rational desire as to the disposition of [his or her] property." *Wilson v. Lane*, 279 Ga. 492, 614 S.E.2d 88 (2005); O.C.G.A. § 53–4–11(a). Indeed, testamentary capacity may be possessed by weak-minded or feeble individuals. *Id*. at 492, 614 S.E.2d 88. And "anything less than a total absence of mind does not destroy [testamentary] capacity." *Griffin v. Barrett*, 183 Ga. 152, 164, 187 S.E. 828 (1936).

Georgia law expressly recognizes two conditions that may destroy or at least limit an individual's testamentary capacity. These are insanity and monomania. O.C.G.A. § 53-4-11(c). However, even an insane individual can make a will during a “lucid interval” as long as the wishes of the testator expressed in the will have been biased by the insanity. O.C.G.A. § 53-4-11(c). A “lucid interval” is not a medical term, but rather a legal term that describes a time in which an individual who is otherwise insane possesses sufficient understanding to form the requisite decided and rational desire to make a valid will. *Scott v. Gibson*, 194 Ga. 503, 22 S.E.2d 51 (1942); *Anderson v. Anderson*, 210 Ga. 464, 80 S.E.2d 807 (1954).

O.C.G.A. § 53-12-25 sets forth how property may be transferred to a trust:

> (a) Transfer of property in trust shall require a transfer of legal title to the trustee. In any transfer of property or any interest in property, if a trust is named as a grantee, whether such trust is held under the laws of this state or of any other jurisdiction, then such transfer is deemed to have been made to the trustee of such trust as though the trustee of such trust had been named as grantee instead of the trust.
>
> (b) For any interest in real property to become trust property in a trust of which any transferor is a trustee, the instrument of conveyance shall additionally be recorded in the appropriate real property records.

O.C.G.A. § 53-12-25.

III. **<u>Duties and Responsiblites to a Trust</u>**

O.C.G.A. § 53-12-261 specifically sets forth the powers of trustees, and provides as follows:

> (a) As used in this Code section, the term "fiduciary" means the one or more personal representatives of the estate of a decedent or the one or more

trustees of a testamentary or inter vivos trust, whichever in a particular case is appropriate.

(b) A trustee of an express trust, without court authorization, shall be authorized:

(1) To sell, exchange, grant options upon, partition, or otherwise dispose of any property or interest therein which the fiduciary may hold from time to time, at public or private sale or otherwise, with or without warranties or representations, upon such terms and conditions, including credit, and for such consideration as the fiduciary deems advisable and to transfer and convey the property or interest therein which is at the disposal of the fiduciary, in fee simple absolute or otherwise, free of all trust. The party dealing with the fiduciary shall not be under a duty to follow the proceeds or other consideration received;

(2) To invest and reinvest in any property which the fiduciary deems advisable, including, but not limited to, common or preferred stocks, bonds, debentures, notes, mortgages, or other securities, in or outside the United States; insurance contracts on the life of any beneficiary or of any person in whom a beneficiary has an insurable interest or in annuity contracts for any beneficiary; any real or personal property; investment trusts, including the securities of or other interests in any open-end or closed-end management investment company or investment trust registered under the federal Investment Company Act of 1940, 15 U.S.C. Section 80a-1, et seq.; and participations in common trust funds;

(3) To the extent and upon such terms and conditions and for such periods of time as the fiduciary shall deem necessary or advisable, to continue or participate in the operation of any business or other enterprise, whatever its form or organization, including, but not limited to, the power:

(A) To effect incorporation, dissolution, or other change in the form of the organization of the business or enterprise;

(B) To dispose of any interest therein or acquire the interest of others therein;

(C) To contribute or invest additional capital thereto or to lend money thereto in any such case upon such terms and conditions as the fiduciary shall approve from time to time; and

(D) To determine whether the liabilities incurred in the conduct of the business are to be chargeable solely to the part of the trust set aside for use in the business or to the trust as a whole.

In all cases in which the fiduciary is required to file accounts in any court or in any other public office, it shall not be necessary to itemize receipts, disbursements, and distributions of property; but it shall be sufficient for the fiduciary to show in the account a single figure or consolidation of figures, and the fiduciary shall be permitted to account for money and property received from the business and any payments made to the business in lump sum without itemization;

(4) To form a corporation or other entity and to transfer, assign, and convey to the corporation or entity all or any part of the trust property in exchange for the stock, securities, or obligations of or other interests in any such corporation or entity and to continue to hold the stock, securities, obligations, and interests;

(5) To continue any farming operation and to do any and all things deemed advisable by the fiduciary in the management and maintenance of the farm and the production and marketing of crops and dairy, poultry, livestock, orchard, and forest products, including, but not limited to, the power:

(A) To operate the farm with hired labor, tenants, or sharecroppers;

(B) To lease or rent the farm for cash or for a share of the crops;

(C) To purchase or otherwise acquire farm machinery, equipment, and livestock;

(D) To construct, repair, and improve farm buildings of all kinds needed, in the fiduciary's judgment, for the operation of the farm;

(E) To make or obtain loans or advances at the prevailing rate or rates of interest for farm purposes, such as for production, harvesting, or marketing; or for the construction, repair, or improvement of farm buildings; or for the purchase of farm machinery, equipment, or livestock;

(F) To employ approved soil conservation practices, in order to conserve, improve, and maintain the fertility and productivity of the soil;

(G) To protect, manage, and improve the timber and forest on the farm and to sell the timber and forest products when it is to the best interest of the trust;

(H) To ditch, dam, and drain damp or wet fields and areas of the farm when and where needed;

(I) To engage in the production of livestock, poultry, or dairy products and to construct such fences and buildings and to plant pastures and crops as may be necessary to carry on such operations;

(J) To market the products of the farm; and

(K) In general, to employ good husbandry in the farming operation;

(6) To manage real property:

(A) To improve, manage, protect, and subdivide any real property;

(B) To dedicate, or withdraw from dedication, parks, streets, highways, or alleys;

(C) To terminate any subdivision or part thereof;

(D) To borrow money for the purposes authorized by this paragraph for the periods of time and upon the terms and conditions as to rates, maturities, and renewals as the fiduciary shall deem advisable and to mortgage or otherwise encumber the property or part thereof, whether in possession or reversion;

(E) To lease the property or part thereof, the lease to commence at the present or in the future, upon the terms and conditions, including options to renew or purchase, and for the period or periods of time as the fiduciary deems advisable even though the period or periods may extend beyond the duration of the trust;

(F) To make gravel, sand, oil, gas, and other mineral leases, contracts, licenses, conveyances, or grants of every nature and kind which are lawful in the jurisdiction in which the property lies;

(G) To manage and improve timber and forests on the property, to sell the timber and forest products, and to make grants, leases, and contracts with respect thereto;

(H) To modify, renew, or extend leases;

(I) To employ agents to rent and collect rents;

(J) To create easements and to release, convey, or assign any right, title, or interest with respect to any easement on the property or part thereof;

(K) To erect, repair, or renovate any building or other improvement on the property and to remove or demolish any building or other improvement in whole or in part; and

(L) To deal with the property and every part thereof in all other ways and for such other purposes or considerations as it would be lawful for any person owning the same to deal with the property either in the same or in different ways from those specified elsewhere in this paragraph;

(7) To lease personal property of the trust or part thereof, the lease to commence at the present or in the future, upon the terms and conditions, including options to renew or purchase, and for the period or periods of time as the fiduciary deems advisable even though the period or periods may extend beyond the duration of the trust;

(8) (A) To pay debts, taxes, assessments, compensation of the fiduciary, and other expenses incurred in the collection, care, administration, and protection of the trust; and

(B) To pay from the trust all charges that the fiduciary deems necessary or appropriate to comply with laws regulating environmental conditions and to remedy or ameliorate any such conditions which the fiduciary determines adversely affect the trust or otherwise are liabilities of the trust and to apportion all such charges among the several bequests and trusts and the interests of the beneficiaries in such manner as the fiduciary deems fair, prudent, and equitable under the circumstances;

(9) To receive additional property from any source and to administer the additional property as a portion of the appropriate trust under the management of

the fiduciary, provided that the fiduciary shall not be required to receive the property without the fiduciary's consent;

(10) In dealing with one or more fiduciaries of the estate or any trust created by the decedent or the settlor or any spouse or child of the decedent or settlor and irrespective of whether the fiduciary is a personal representative or trustee of such other estate or trust:

(A) To sell real or personal property of the estate or trust to such fiduciary or to exchange such property with such fiduciary upon such terms and conditions as to sale price, terms of payment, and security as shall seem advisable to the fiduciary; and the fiduciary shall be under no duty to follow the proceeds of any such sale; and

(B) To borrow money from the estate or trust for such periods of time and upon such terms and conditions as to rates, maturities, renewals, and securities as the fiduciary shall deem advisable for the purpose of paying debts of the decedent or settlor, taxes, the costs of the administration of the estate or trust, and like charges against the estate or trust or any part thereof or of discharging any other liabilities of the estate or trust and to mortgage, pledge, or otherwise encumber such portion of the estate or trust as may be required to secure the loan and to renew existing loans;

(11) To borrow money for such periods of time and upon such terms and conditions as to rates, maturities, renewals, and security as the fiduciary shall deem advisable for the purpose of paying debts, taxes, or other charges against the trust or any part thereof and to mortgage, pledge, or otherwise encumber such portion of the trust as may be required to secure the loan and to renew existing loans either as maker or endorser;

(12) To make loans or advances for the benefit or the protection of the trust;

(13) To vote shares of stock or other ownership interests owned by the trust, in person or by proxy, with or without power of substitution;

(14) To hold a security in the name of a nominee or in other form without disclosure of the fiduciary relationship, so that title to the security may pass by

delivery; but the fiduciary shall be liable for any act of the nominee in connection with the security so held;

(15) To exercise all options, rights, and privileges to convert stocks, bonds, debentures, notes, mortgages, or other property into other stocks, bonds, debentures, notes, mortgages, or other property; to subscribe for other or additional stocks, bonds, debentures, notes, mortgages, or other property; and to hold the stocks, bonds, debentures, notes, mortgages, or other property so acquired as investments of the trust so long as the fiduciary shall deem advisable;

(16) To unite with other owners of property similar to any which may be held at any time in the trust, in carrying out any plan for the consolidation or merger, dissolution or liquidation, foreclosure, lease, or sale of the property or the incorporation or reincorporation, reorganization, or readjustment of the capital or financial structure of any corporation, company, or association the securities of which may form any portion of an estate or trust; to become and serve as a member of a shareholders' or bondholders' protective committee; to deposit securities in accordance with any plan agreed upon; to pay any assessments, expenses, or sums of money that may be required for the protection or furtherance of the interest of the beneficiaries of any trust with reference to any such plan; and to receive as investments of the trust any securities issued as a result of the execution of such plan;

(17) To adjust the interest rate from time to time on any obligation, whether secured or unsecured, constituting a part of the trust;

(18) To continue any obligation, whether secured or unsecured, upon and after maturity, with or without renewal or extension, upon such terms as the fiduciary shall deem advisable, without regard to the value of the security, if any, at the time of the continuance;

(19) To foreclose, as an incident to the collection of any bond, note, or other obligation, any deed to secure debt or any mortgage, deed of trust, or other lien securing the bond, note, or other obligation and to bid in the property at the foreclosure sale or to acquire the property by deed from the mortgagor or obligor

without foreclosure; and to retain the property so bid in or taken over without foreclosure;

(20) To carry such insurance coverage as the fiduciary shall deem advisable;

(21) To collect, receive, and issue receipts for rents, issues, profits, and income of the trust;

(22) (A) To compromise, adjust, mediate, arbitrate, or otherwise deal with and settle claims involving the trust or the trustee;

(B) To compromise, adjust, mediate, arbitrate, bring or defend actions on, abandon, or otherwise deal with and settle claims in favor of or against the trust as the fiduciary shall deem advisable; the fiduciary's decision shall be conclusive between the fiduciary and the beneficiaries of the trust and the person against or for whom the claim is asserted, in the absence of fraud by such persons and, in the absence of fraud, bad faith, or gross negligence of the fiduciary, shall be conclusive between the fiduciary and the beneficiaries of the trust; and

(C) To compromise all debts, the collection of which are doubtful, belonging to the trust when such settlements will advance the interests of those represented;

(23) To employ and compensate, out of income or principal or both and in such proportion as the fiduciary shall deem advisable, persons deemed by the fiduciary needful to advise or assist in the administration of any trust, including, but not limited to, agents, accountants, brokers, attorneys at law, attorneys in fact, investment brokers, rental agents, realtors, appraisers, and tax specialists; and to do so without liability for any neglect, omission, misconduct, or default of the agent or representative, provided such person was selected and retained with due care on the part of the fiduciary;

(24) To acquire, receive, hold, and retain undivided the principal of several trusts created by a single trust instrument until division shall become necessary in order to make distributions; to hold, manage, invest, reinvest, and account for the several shares or parts of shares by appropriate entries in the fiduciary's books of account and to allocate to each share or part of share its

proportionate part of all receipts and expenses; provided, however, that this paragraph shall not defer the vesting in possession of any share or part of share of the trust;

(25) To set up proper and reasonable reserves for taxes, assessments, insurance premiums, depreciation, obsolescence, amortization, depletion of mineral or timber properties, repairs, improvements, and general maintenance of buildings or other property out of rents, profits, or other income received;

(26) To value assets of the trust and to distribute them in cash or in kind, or partly in cash and partly in kind, in divided or undivided interests, as the fiduciary finds to be most practical and in the best interest of the distributees, the fiduciary being able to distribute types of assets differently among the distributees;

(27) To transfer money or other property distributable to a beneficiary who is under age 21, an adult for whom a guardian or conservator has been appointed, or an adult who the fiduciary reasonably believes is incapacitated by distributing such money or property directly to the beneficiary or applying it for the beneficiary's benefit, or by:

(A) Distributing it to the beneficiary's conservator or, if the beneficiary does not have a conservator, the beneficiary's guardian;

(B) Distributing it to the beneficiary's custodian under "The Georgia Transfers to Minors Act" or similar state law and, for that purpose, creating a custodianship and designating a custodian;

(C) Distributing it to the beneficiary's custodial trustee under the Uniform Custodial Trust Act as enacted in another state and, for that purpose, creating a custodial trust; or

(D) Distributing it to any other person, whether or not appointed guardian or conservator by any court, who shall, in fact, have the care and custody of the person of the beneficiary;

The fiduciary shall not be under any duty to see to the application of the distributions so made if the fiduciary exercised due care in the selection of the

> person, including the beneficiary, to whom the payments were made; and the receipt of the person shall be full acquittance to the fiduciary;
>
> (28) To make, modify, and execute contracts and other instruments, under seal or otherwise, as the fiduciary deems advisable; and
>
> (29) To serve without making and filing inventory and appraisement, without filing any annual or other returns or reports to any court, and without giving bond; but, in addition to any rights the beneficiaries may have under subsection (b) of Code Section 53-12-243, the fiduciary shall furnish to the income beneficiaries, at least annually, a statement of receipts and disbursements.

A fiduciary duty is the highest duty known in the law. Mary F. Radford, Georgia Trusts and Trustees, § 9:1, p. 349 (2015-2016 Ed.). Chief Justice Benjamin Cardozo's opinion in Meinhard v. Salmon, 249 N.Y. 458, 464, 164 N.E. 545 (1928) explained the exacting standard of undivided loyalty that is required as follows:

> Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts or equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions.

Georgia law similarly states that a trustee "shall administer the trust in good faith, in accordance with its provisions and purposes." O.C.G.A. § 53-12-240(b). Even if a trust grants the trustee unlimited discretion, the trustee "shall exercise a discretionary power in good faith." O.C.G.A. § 53-12-260. A testamentary trustee must act for the benefit of the trust estate "but also in such a way as not to gain any advantage, directly or indirectly . . . and he owes an undivided duty to the beneficiary, and must not place himself in a position where his personal interest will conflict with the interest of the beneficiary." Hanson v. First State Bank & Trust Co., 259 Ga.

710, 711, 385 S.E.2d 266, 267 (1989) (quoting Clark v. Clark, 167 Ga. 1, 405, 144 S.E. 787 (1928)). "The purpose of this rule is to require a trustee to maintain a position where his every act is above suspicion, and the trust estate, and it alone, can receive, not only his best services, but his unbiased and uninfluenced judgment." Id. The duty as applied to personal representatives of estates is equally demanding. "An administrator (or executor) is administrative representative of the deceased, with property and testamentary rights. [The fiduciary] is a quasi court officer and has the sacred duty of standing in the place of the deceased and administering the estate as directed…. [The fiduciary] is a trustee invested with a solemn trust to manage the estate under his control to the best advantage of those interested in it.... Nothing can be tolerated which comes into conflict or competition with the interests and welfare of those interested in the estate." Ringer v. Lockhart, 240 Ga. 82, 84-85, 239 S.E.2d 349, 351 (1977) (citations omitted).

IV. Revocable vs. Irrevocable

A trust can be revocable or irrevocable. A revocable trust is a trust which by its express terms can be revoked by the settlor. The power to revoke a trust includes the power to modify a trust. An unrestricted power to modify a trust is deemed to include a power to modify a trust. O.C.G.A. § 53-12-40. A settlor's agent may revoke a revocable trust if the agent is expressly authorized to do so under a power of attorney. O.C.G.A. § 53-12-43(a). For income tax purposes, a revocable trust is treated as the alter ego of the settlor. It does not file a separate tax return. Its income and deductions flow through to the settlor's personal tax return and are reported under the settlor's social security number. Revocable trusts are generally used because they are an easy method for transferring assets at death in order to avoid probate.

An irrevocable trust is a trust which is not revocable by the settlor. However, even though a trust may be irrevocable, it may be possible to be terminated or modified by other means. These actions include an action under the Georgia modification statutes, termination of an uneconomic trust under the terms of the trust instrument, and the exercise of general power of appointment. Depending on the other characteristics of the trust, the assets of an irrevocable trust may also be available for distribution. An irrevocable trust is often used as a method of tax planning, creditor protection, or disability planning.

O.C.G.A. § 53-12-60 sets forth how an irrevocable trust may be reformed by a court:

> (a) If it is proved by clear and convincing evidence that the trust provisions were affected by a mistake of fact or law, whether in expression or inducement, the court may reform the trust provisions, even if unambiguous, to conform the provisions to the settlor's intention.
>
> (b) A petition for reformation may be filed by the trustee or any beneficiary or, in the case of an unfunded testamentary trust, the personal representative of the settlor's estate.
>
> (c) Notice of a petition for reformation of the trust shall be given to the trustee and all beneficiaries.

V. <u>Determining your client's planning needs.</u>

In the initial meeting, clients should be encouraged to collect the personal and financial data necessary to help them with their planning needs. The client should be asked to bring all deeds and other documents of title, life insurance policies, and retirement plan information. Life insurance and retirement plan beneficiary information should also be brought for review.

A lawyer should use the initial conference with the client for several purposes. First, to collecting basic data needed to assist the client, which includes the above documents. The lawyer needs to then attempt to ascertain the dispositive intent of the client, which goes beyond just who they want to receive the assets of their estate. Some examples of considerations are the following:

- How will the client and their spouse's financial needs be met in the event of disability?
- How is the client going to protect the assets for the children in the event that the surviving spouse remarries?
- Are there any special needs of the children that need to be considered?
- Are the children old enough to receive an inheritance outright?
- Who does the client intend to benefit from the creation of the trust?
- What is the goal of creating the trust?
- How much authority does the client wish to grant to the trustee?
- Who should be selected as the trustee and why?
- What power should the beneficiaries have to change the directions set forth in the trust instrument?
- What should each beneficiaries interest in the trust be?

The goal of the initial meeting is to fully determine the client's dispositive intent. A trust can have a single beneficiary or multiple beneficiaries. Similarly, a trust can have a single trustee or multiple trustees acting as co-trustees. A beneficiary can serve as a trustee or co-trustee. However, a family member that is not a beneficiary is most often named as trustee for impartiality purposes.

A trust may contain one or more powers of appointment, which is nothng more than the beneficiaries right pursuant to the trust to change certain directions of the trust. A power of appointment can be exercised to cut out beneficiaries, change how and when beneficiaries receive trust property, as well as to add beneficiaries. The settlor generally defines the scope of this power, including the people and charities that may be named to receive trust property. Powers of appointment are routinely included for high net worth clients who create irrevocable trusts to provide flexibility and avoid tax issues.

VI, Determining which type of trust to use.

Determining which type of trust to use is entirely dependent upon the client's needs and goals, which need to be ascertained in the initial meeting with the client. Trusts can accomplish a range of goals, including avoiding probate, minimizing estate taxes, and making sure your client's heirs receive as much of the client's money as possible as quickly as possible. The following are some types of trusts often used in estate planning:

A. Qualified Personal Residence Trust (QPRT): A QPRT is a product of Section 2702 of the Internal Revenue Code. It is an irrevocable trust created by the settlor to own an interest in the settlor's primary residence or vacation home. The settlor retains the right to occupy the residence for a set term of years. At the end of the term if the settlor is living, the property passes to the specified remainder beneficiaries. If the trustee sells the home during the term of the trust and the trust does not buy a replacement property, the trustee is required to pay an annuity for the balance of the trust term which is calculated to replace the value of the settlor's right to remain in the residence. If the settlor dies during the term of the trust, the property passes pursuant to the settlor's will.

B. Grantor Retained Annuity Trust (GRAT): A GRAT is similar to a QPRT as it is subject to the narrow restrictions of Section 2702 of the Internal Revenue Code. A GRAT is an irrevocable trust created by a single settlor to which the settlor transfers assets and retains the right to receive an annuity from the trust each year for the term of the trust. If the settlor survives the terms of the trust, any assets remaining n the trust will be distributed to the remainder beneficiaries. If the settlor fails to survive the term, the property remaining in the GRAT is generally distributed to the settlor's estate.

C. Charitable Remainder Trust (CRT): A CRT s an irrevocable trust to which the sellor transfers assets and retains the right to receive an annuity each year for either the settlor's lifetime or a set term of years. At the end of the term, whether the term ends with the death of the settlor or a number of years, the remaining assets are distributed to charity.

D. Irrevocable Insurance Trust (ILIT): An ILIT is an irrevocable trust created by the settlor to own insurance on the settlor's life so the death benefit s not included in the settlor's estate at his or her death. The trust is usually for the benefit of the settlor's spouse and children with a provision to treat the beneficiary spouse as predeceased in the event of a divorce. On divorce, the beneficiary spouse would cease automatically to be included as a beneficiary.

E. Spousal Access Trust (SLAT): A SLAT is an irrevocable trust created by a settlor spouse under which the other spouse is a beneficiary with the couple's descendants. The theory is that the trustee can make distributions to the spouse beneficiary to provide for the couple's lifestyle. Some SLAT's provide for distribution of all income to the spouse, while others provide for discretionary income.

F. Credit Shelter Trust (CST): A CST is designed to allow affluent couples to reduce or completely avoid estate taxes when passing along assets to their heirs. This type of irrevocable trust is structured so that upon the death of the settlor, the assets specified in the trust agreement and the income they generate are transferred to the settlor's spouse. A key benefit to this type of trust is that the surviving spouse maintains certain rights to the trust assets during their lifetime. Upon the surviving spouse's death, the trust's assets are distributed to the remaining beneficiaries without any estate taxes being levied.

G. Qualifed Terminable Interest Trusts (QTIP): A QTIP enables the grantor to provide for a surviving spouse and maintain control of how the trust's assets are distributed once the surviving spouse dies. Income, and sometimes principal, generated from the trust is given to the surviving spouse to ensure that the spouse is taken care of for the rest of their life. This type of trust is commonly used by individuals who have children from another marriage, and enable the settlor to look after their current spouse while making sure that the assets are passed onto beneficiaries of his or her choice, usually children from a prior marriage.

Revocable Living Trusts

Submitted by Michael Burns

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Trusts 101

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Revocable Living Trusts

A. Traditional Estate Planning vs. Revocable Living Trusts

Revocable trust planning is a popular tool used by estate planning attorneys to achieve a variety of goals including providing a mechanism for disability management, safeguarding privacy, ensuring effective post-mortem transfer of property, and probate avoidance. The most popular reason for utilizing a revocable living trust plan is probate avoidance, whether in an individual's home state (domiciliary probate) or to avoid probate in an out-of-state jurisdiction where real property is owned (ancillary probate). Depending on the state and jurisdiction, practitioners often have a strong preference either for or against the use of revocable trusts. In reality, a number of factors need to be taken into account in advising respective clients, as there is no one size fits all in estate planning.

Probate Avoidance

The reason to bypass probate is often the desire to avoid the cost and formality of the probate process. Such costs and formalities vary significantly by jurisdiction and state. For example, in Florida, there are minimum statutory fees for attorneys and significant savings can be realized through a properly funded revocable revocable trust. In contrast, in Georgia, assuming a property drafted Will, the probate process is relatively simple and the cost savings are typically minor. Each practitioner should understand his or her state’s statutory and customary fees including, but not limited to, the commissions of the executor or administrator, attorney's fees, guardians ad litem fees, court costs, and whether the accounting and inventory are waivable.

In addition to cost savings, the use of a revocable trust can be especially important where an individual is worried about a potential Will contest or has heirs that are unknown or not easily located. Most jurisdictions have statutory notice requirements that mandate that all heirs-at-law are provided a copy of the Will and probate petition. In other words, where the heirs are unknown, the nominated Executor or Administrator must conduct due diligence or hire an outside company in order to determine the address and relation for each heir.

> **Example:** Janice Smith, a ninety-five year old Georgia resident, had a valid Will leaving all of her assets to her husband, if living, and, if not, to a local charity. Janice’s husband predeceased her, they had no children, and her closest heirs-at-law were distant relatives. Upon Janet’s passing, the nominated Executor would need to determine the heirs and each of their respective addresses in order for the court to serve process. This could represent a significant delay to the estate and potentially a large hidden cost. However, if Janet were able to bypass probate through the use of a revocable trust and beneficiary designations, this would alleviate the delay and potential cost.

Additionally, where an heir is disinherited, service of process by the court can serve as notice or a reminder for the heir to file a caveat, especially where the heir was estranged or the estate is large. Even if such caveat is a nuisance claim, it could delay estate administration and entice the executor or administrator in to seeking a settlement. However, if probate is avoided, it is unlikely the heir would ever learn of the decedent's passing or determine how to properly contest the revocable trust.

Probate can be avoided entirely by having no assets in the deceased's name (i.e. each asset is owned by a revocable trust, passes via beneficiary designation or joint ownership, or some other form of transfer) or an individual can seek to have certain assets avoid probate. As briefly discussed above, even in jurisdictions that have a simple domiciliary probate process, a revocable trust may be an especially useful vehicle to avoid expensive ancillary probate proceedings.

> **Example:** John Smith, a resident of Georgia, owns real property in Florida, California, and Texas. If John were to pass away owning the property in his name individually, domiciliary probate would occur in Georgia and ancillary probate would occur in Florida, California, and Texas. However, if John Smith owned the property in a properly administered revocable trust, ancillary probate would be avoided and the property could be transferred via the terms of the revocable trust.

On the negative side, avoiding the probate process bypasses certain safeguards built into each state's law to prevent potential fraud and other unintended consequences. Such safeguards include judicial supervision of the estate administration process and the Will Act Formalities. In most jurisdictions, those safeguards will not apply with respect to property passing by a revocable trust. While most clients or practitioners see the lack of judicial supervision as beneficial, there are circumstances in which such lack of supervision is harmful to the overall estate plan.

Privacy

The revocable trust may offer advantages for an individual seeking privacy. Since a property owner's Will and, in some cases, the assets, may be a matter of public record, an individually wishing to maintain confidentiality with respect to the nature of dispositions and assets should utilize a revocable trust. This is especially important for many public figures including politicians, celebrities, and athletes. It seems there is a story each month in the New York Times or Wall Street Journal publicizing the terms of a celebrity's Will. If the celebrity had instead utilized a revocable trust, such publicity (often negative) could have been avoided.

> **Example:** Joe Cobb, a famous musician and resident of Georgia, has numerous children from prior relationships that the public is unaware of. Joe seeks to provide for each of the children under the terms of his estate planning documents, but it is foremost desire that the children's identity be kept secret in order to preserve their lifestyle. If Joe utilizes a pour-over will and revocable trust, only the barebones Will would be required to be filed with the court and the revocable trust would remain private.

Disability Management

Executing and funding a properly drafted revocable trust is most likely the best way to ensure a grantor's property remains available to be used for his or her benefit in the event of a physical or mental impairment. There is little to no interruption in asset management and the successor trustee may act immediately to ensure care is provided. While a durable power of attorney offers similar benefits, third parties such as banks and financial institutions often have more difficulty in dealing with a power of attorney than a trust agreement. Additionally, depending on state law, a bank or financial institution may not be required to accept the power of attorney or there may be a lengthy process in order for it to be accepted.

Effective Transfer of Property at Passing

Similar to disability management, there may be a need to ensure continuity of management upon a grantor's passing. By utilizing a revocable trust, the grantor is able to nominate a successor trustee to have immediate (or nearly immediate) access to the grantor's assets upon passing. This can be extremely important where the assets include a closely held business, significant real property holdings, or a vast investment portfolio.

> **Example:** Kevin Dole, a Georgia resident and real estate investor, passed away ten days before the closing of a major commercial property. The closing was required for Kevin to avoid a foreclosure on the property. If the property was owned in a revocable trust, the successor trustee would be able to close on the transaction. However, if the property was owned in Kevin's individual name, it would likely take weeks before an executor was appointed.

Revocable trusts can be powerful tools in financial and estate planning. In most cases, especially for affluent clients, significant cost and time savings and other valuable objectives can be achieved. However, there is an additional expense and complexity in creating and funding a revocable trust. In most cases, practitioners should do a client-by-client analysis or even asset-by-asset analysis, as to whether a revocable trust is appropriate to implement.

B. <u>Credit Shelter Trusts</u>

C. <u>Marital Deduction Trusts</u>

D. <u>Qualified Terminable Interest Trusts</u>

Within a revocable trust or will, married couples often have a choice as to how a spouse will inherit the property. Traditional estate tax planning would include a bypass trust (often referred to as a credit shelter trust) for the estate tax exemption amount with the remainder passing to a marital trust. The bypass trust is designed to avoid an estate tax upon the surviving spouse's death and would not receive a basis step-up to fair market value upon the death of the surviving spouse. The marital trust would be taxable to the surviving spouse's estate and thus would receive a step-up in basis to the fair market value as of the date of death. Some advantages of the traditional estate plan include, but are not limited to, the following:

Asset Protection. Assuming properly drafted and subject to state law, the bypass trust will provide some level of asset protection in the event of future marriage, future divorce, or other creditor issues. Proper drafting can also ensure the surviving spouse does not divert the assets to an unintended beneficiary.

> **Example:** John passes away in 2016 leaving all of his assets to a bypass trust for the benefit of his wife, Carol, and his two children. Carol subsequently remarries in 2025 to a con artist, Don, who thinks Carol is worth millions. Don has Carol rewrite her Will leaving all of the assets to Don with the promise that he will provide for the kids. Upon Carol's passing, the assets with the bypass trust would pass to John's children and not Don.

Generation Skipping Tax Transfer ("GST") Planning. While portability provides for the transfer of the deceased spouse's unused estate tax exemption to the surviving spouse, it does not permit transfer of the GST exemption. Accordingly, by funding the bypass trust upon the first spouse to pass, the GST exemption can be preserved so that funds are able to pass in trust from generation to generation. Use of such GST exemption upon the first to pass is crucial to legacy planning. See below regarding the use of a Reverse QTIP election in order to preserve the GST exemption where there is no bypass trust.

Asset Inflation Protection. Proper planning can ensure any growth (inflationary or otherwise) within the bypass trust will avoid future estate taxation. This is because even an inflation-indexed exemption amount would likely obtain less appreciation over time than would be the case with a bypass trust invested in a portfolio allocated for moderate risk.

> **Example:** The stock of A Corporation is transferred to a bypass trust upon the first spouse to die. The stock value subsequently grows from a value of $5,000,000 to $10,000,000. Assuming the surviving spouse has a taxable estate of his or her own and an estate tax rate of 40%, the use of the bypass trust saved $2,000,000 in estate taxation ($5,000,000 * 40% tax rate). However, please note that the stock would not receive a step-up in basis.

> **Example:** Assume a fifty-year old terminally ill client owns an asset expected to appreciate significantly in future years. The client's revocable trust provides a formula gift into a bypass trust. While the asset would receive a step-up in basis at the death of the terminally ill spouse, the estate tax benefits of the formula gift should be weighed against the income tax benefits of having the asset pass outright to the surviving spouse or into a trust where the surviving spouse has a general power of appointment. The practitioner should also take into account any income that the asset produces – if the income is going to be distributed annually due to the tax rates on the trust, the estate tax benefit may be minimal.

State Estate Tax Protection. There are currently more than 20 different state estate tax regimes. Planners need to be cognizant of the state estate tax rules governing their clients and whether relying on "portability" could result in an unanticipated state estate tax bill.

> **Example:** John and Carol lived in State A (no state estate tax) at the time of John's death. John had an estate of approximately $2,000,000 that passed directly to Carol. Carol filed an estate tax return to obtain John's unused estate tax exemption. Carol subsequently moves to State B that has a state estate tax of 10%, an exemption of $1,000,000, and does not recognize portability. Upon Carol's passing, the estate will owe $100,000 in state estate taxes to State B ($1,000,000 * 10%). Such tax could have been avoided through the use of a bypass trust.

Investment and Administrative Management. By utilizing a bypass and marital trust, the deceased spouse can ensure the assets are properly managed, either by a corporate trustee or a trusted individual with experience. The Trustee should ensure proper record keeping, engage in tax planning, make decisions objectively, and utilize its expertise in investment allocations. This can be particularly important for elderly clients or clients with complex or difficult family situations.

> **Example:** Dianne, who handled her family's financial affairs, passes away in 2016 at the age of 96 leaving all of her assets outright to her husband, John, who is also 96 years old. John, who is now in charge of managing the investments and ensuring all tax returns are properly handled, falls prey to a scam IRS e-mail and loses a substantial portion of the inheritance.

The permanency of portability and increased estate tax exemptions codified in the American Taxpayer Relief Act of 2012 (ATRA) and the Tax Cuts and Jobs Act of 2017

(TCJA) have resulted in 99.9% of U.S. residents no longer having to worry about the estate tax. As such, the use of a traditional estate tax planning for many clients is no longer necessary. Many clients, even those with a significant net worth, may prefer to rely on portability.

Portability planning is a rather broad concept coined by planners that can range from having all assets pass via joint ownership to the surviving spouse to a complex plan designed to have all assets pass in trust with the spouse making an election to take advantage of the unlimited marital deduction and applicable GST exemption. The basic idea is that by eliminating the risk of losing a portion of all of the estate tax exemption, portability permits a wide array of opportunities in tailoring a plan to the needs of the client.

In reviewing options, a planner should always determine the client's objectives and run an objective math based analysis.

Client Objectives. A thorough review of client objectives should be the basis for planning. Questions include, but are not limited to, the following:

- Determine the level of complexity the client is comfortable with. While relying on portability may be the simplest route in the beginning, is the client comfortable with the expense of timely filing an estate tax return (Form 706)? Discuss with the client that an outright distribution can result in the funds passing to the surviving spouse's new husband or wife and/or his or her respective children.
- Are there asset protection concerns? If there are large contingent liabilities, an outright distribution may result in the funds passing to the creditors of the surviving spouse.
- Review the client's personal financial statement to determine the asset base. For example, if the client has nearly all of his or her net worth in retirement assets and a primary residence, there are potential adverse consequences to having the assets pass

to a bypass trust. This could lead to a loss of tax deferral for the IRA and a potential loss of homestead (or other similar protection) and property tax deductions for the primary residence.

- How are the assets titled? If everything is jointly titled except for relatively low value assets that are difficult to appraise, the purpose of the formula gift to a bypass trust would be defeated and may ultimately become a hindrance when filing the estate tax return.
- Discuss the family dynamic. If the client is in a third marriage with children from the prior two marriages, an outright distribution to the current wife could be a potential for disaster. There also needs to be a thorough discussion of the decision makers – in the situation discussed above, it may be prudent to appoint a corporate or independent trustee in order to lessen distrust and dissension between the family units.
- What is the legacy the client wants to leave? If the client only cares about providing for the spouse, a simple approach may be warranted. However, if the client desires to provide for future generations, the client should maximize GST planning.
- Discuss the charitable intentions of the family. If there will be significant charitable bequests, a different approach may be taken.
- Portability only applies to the last deceased spouse – the client should understand the risk that if the surviving spouse remarries and the new spouse predeceases, the portable exemption may be lost absent gifting.
- Determine the residency and citizenship status of each spouse. If the client is a non-resident alien from a country without an applicable tax treaty, portability may not apply.
- The uncertainty regarding tax laws should be discussed with the client. While ATRA made the estate exemptions and portability "permanent", there is always a chance Congress revises the law. Additionally, the increased exemptions in TCJA are set to sunset in 2025.
- An advisor should review the plan from a tax savings perspective by looking at (1) the time (i.e. life expectancy of each spouse), (2) tax rates and exemptions, and (3)

the anticipated rate of return. In most circumstances, there is a greater economic benefit from the portability plan than the traditional estate plan for clients with a net worth less than the combined exemption rate due to the income tax advantage.

- If someone other than the spouse is being appointed as Executor or Trustee, ensure that the appointed individual timely files the estate tax return in order to elect portability. A provision in the testamentary document should also indicate whether the estate or surviving spouse will be responsible for the cost of such filing.
- Determine whether a trustee of a bypass trust having a spray power among a class of beneficiaries in lower tax brackets can provide tax savings.

In the event the tax and non-reasons for relying on portability planning align with the client's objectives, there are numerous options for the client ranging from a simple testamentary document passing all assets outright to a complex testamentary document that includes a formula gift to Reverse QTIP/ QTIP trusts. A few examples are discussed below:

Disclaimer Tax Planning. If the reasons for establishing a bypass trust (or providing for a distribution to a QTIP trust) are not significant, but the client wants to give the surviving spouse the option of establishing a bypass trust, the estate plan can provide for an outright distribution to the surviving spouse with such spouse having the ability to "disclaim" all or a portion the inheritance to a disclaimer or bypass trust. The decision to disclaim must be made during the nine-month period following the first spouse's death. One caveat is that the surviving spouse cannot have a power of appointment over the disclaimed assets.

> **Example:** Assume John and Carol are a young married couple and that John has a net worth of approximately $2,000,000. John does not want to do any advanced planning other than a simple Will that provides for an outright distribution to Carol. Subsequently, there is a car accident

where John is killed and Carol is incapacitated. If a disclaimer trust is included in John's testamentary document and the power to disclaim is included in Carol's durable general power of attorney, there could be some asset protection and management for Carol. As a caveat, it is important to review state law.

QTIP Trust. In recommending a client utilize a bypass trust, many advisors cite (i) non-tax reasons including asset protection via a spendthrift clause, asset management, and control over distributions, and (ii) tax reasons such as utilizing the deceased spouse's GST exemption and providing inflation protection from the estate tax.

However, the author believes that many of these concerns can be addressed through the use of a Reverse QTIP/QTIP trust. A testamentary document that provides for the use of a QTIP trust would permit the deceased spouse to designate control over the distribution of the trust assets upon the death of the surviving spouse, preserve the deceased spouse's GST exemption through a "reverse QTIP election," and provide a greater degree of creditor protection than would be permitted by an outright bequest to the surviving spouse.

Utilizing a QTIP Trust to accomplish these objectives may allow the trust assets to step-up to fair market value upon the death of the surviving spouse and postpone payment of state level estate taxes until the death of the surviving spouse in certain situations. In addition, by electing portability, the surviving spouse can utilize the deceased spouse's unused estate tax exemption in making tax-free gifts. While there has been uncertainty for the last six years regarding the validity of a qualified "QTIP" election made solely to allow for the use of portability due to Revenue Procedure 2001-38, Revenue Procedure 2016-49, effective as of September 27, 2016, makes clear that a QTIP election can be used along with a portability election, even in cases where the QTIP election was not needed to reduce or eliminate estate taxes at the first spouse's death.

The changes in the American Taxpayer Relief Act of 2012 the Tax Cuts and Jobs Act of 2017 have not simplified estate planning. ATRA and TCJA made estate planning significantly more complex and increased the potential exposure of advisors and fiduciaries that do not pay sufficient attention to income tax and tax basis issues in their decisions, planning, and advice. Advisors will need to have a better understanding of client objectives in order to craft an effective estate plan. Advisors should also have a deep understanding of how portability works and how it can be integrated into a client's estate plan.

E. <u>Funding the Trust</u>

F. <u>Drafting Tips and Samples</u>

In funding a revocable trust, it is important that the revocable trust is sufficiently identified and each asset correctly titled. The format is typically some variation of "John Doe, as Trustee of John Doe's Revocable Trust dated _________, 2018, as amended from time to time". Each bank or other financial institution may require slightly different wording, but as long as your trust is clearly identified, there is no issue with such variation. In most jurisdictions, since the Trustee is the owner of the assets (albeit as a custodian) and not the Trust itself, it is important that the Trustee is identified in the title.

Beneficiary Designations for Retirement Plan Accounts

The tax law requires that a retirement benefit death plan that is not paid to a surviving spouse of the plan participant must be distributed within five years after the death of the participant or begin within one year of the death of the participant and continue over the lifetime of the "designated beneficiary", but only individuals can be designated beneficiaries. In other words, if the revocable trust is named, there can be adverse tax consequences. The use of conduit and accumulation trusts within a revocable trust is outside the scope of this article.

Brokerage and Bank Accounts

In order to fully fund a revocable trust, a grantor should transfer brokerage or checking account revocable trust. The wording indicated above should be sufficient. In the event a successor trustee needs to take over as a result of the death, resignation, or incapacity of the grantor, the successor trustee will need to provide

Life Insurance

A grantor will typically want to name the revocable trust as the beneficiary of any life insurance policy.

Closely Held Business Interests

A grantor may (or may not) be able to transfer any closely held business interest to his or her revocable trust. The practitioner should request a copy of the business's operating documents (i.e. shareholder's agreement for a corporation, operating agreement for LLC, etc.) to see if it is permitted and if it is permitted, exactly what formalities need to be followed. Any corporate interest is typically transferred via stock certificate and any LLC or partnership interest is transferred via assignment. There will typically be a fee charged by the business for such transfer.

Real Property

The wording indicated above should be used on deeds to real property that will be transferred to a revocable trust. Recording fees may be charged to transfer real estate, but there is a typically a transfer tax exemption in most states. If there is a mortgage on the property, you should contact the mortgage holder to obtain approval for such transfer assuming there is a due on transfer clause in the mortgage agreement. The client should also ensure that any home insurance is changed to reflect the new insured.

Automobiles and Personal Effects

Depending on state law, tangible personal property (e.g., motor vehicles, clothing, jewelry, furniture etc.) is not typically transferred to a trust. Such assets, unless they have very substantial value, tend to be distributed without formal probate proceedings. However, where there is a disposition in the Will that contradicts the terms of a Revocable Trust or where such property has significant value, it is recommended that there is an assignment of such property to the trust.

Taxpayer Identification Number

The Federal taxpayer identification number for the grantor's revocable trust is typically his or her Social Security Number. It is possible to obtain a separate tax identification number for the trust (and may be required where the grantor is no longer serving as Trustee), but this may cause issues with tax reporting. Funding the revocable trust will not and should not change the tax reporting on a grantor's tax return.

G. <u>Common Mistakes to Avoid</u>

Below are some of the biggest mistakes the author has seen, whether by act or omission, that resulted in adverse consequences to clients.

- Not utilizing a revocable trust
- Failing to fund the revocable trust
- Providing blanket assignments to revocable trust and failing to properly fund
- Improperly titling or failing to sufficiently identify the revocable trust
- Designating the revocable trust as beneficiary of a retirement account without proper tax planning
- Providing outright bequests to irresponsible or disabled heirs
- Failing to provide trustee removal and appointment provisions
- Not providing sufficient flexibility within testamentary trusts including failing to include powers of appointment
- Failing to provide sufficient post-disability or post-death liquidity

- Not adequately planning or providing information regarding personal guarantees
- Relying solely on a revocable trust and not providing a pour-over Will and powers of attorney
- Not providing for a common disaster or takers of last resort provision
- Failing to file a 645 election for the Revocable Trust

H. Tax Consequences

Section 645 Election

One of the most common elections on a Form 1041 is a section 645 election to treat a qualified revocable trust (the "Revocable Trust") as owned by the decedent. In most cases, the primary reason for a Revocable Trust to avoid probate. When a grantor of an Revocable Trust dies, the Revocable Trust becomes irrevocable at death and requires a separate taxpayer identification number and income tax return. Since trusts are required to use a calendar year end, unlike estates, there can be two different returns for the decedent's assets due at two different times.

> ***Example:*** John passed away on April 16, 2017 with a brokerage account that is titled in the name of his Revocable Trust and a rental property in his individual name. The trust income tax return (Form 1041) will be due on April 15, 2018 for income earned in the brokerage account between April 17, 2017 and December 31, 2018. The estate income tax return (Form 1041), which elected a fiscal year end of March 31, 2018, will be due on August 15, 2018, for income earned on the rental property between April 17, 2017 and March 31, 2018.

However, where the decedent has both a Revocable Trust and a probate estate, the section 645 election allows the trustee and the executor to effectively combine the Revocable

Trust and estate into one tax return, filed as an estate. Further, even if there is no separate probate estate, this election can be used to file the trust return as though the trust were an estate.

The section 645 election is valid for two years following the decedent's date of death, so the practitioner must also consider the anticipated length of trust and/or estate administration before making the election.

In making the election, certain tax planning advantages are gained by filing as an estate, rather than as a trust – (i) the benefits of utilizing a fiscal year (see additional discussion on Selection of Tax Year above); (ii) the material participation requirement for the passive loss rules is waived (see additional discussion of passive activity losses and basis adjustment above); (ii) the charitable set-aside deduction under Sec. 642(c) is permitted;

> ***Example:*** John passed away on April 16, 2017 with a brokerage account that is titled in the name of his Revocable Trust and a rental property in his individual name. The executor timely files a section 645 election in order to treat the Revocable Trust as part of the estate and elects a fiscal year. A single estate income tax return (Form 1041), with an elected fiscal year end of March 31, 2018, would be due on August 15, 2018, for income earned on the rental property and brokerage account between April 17, 2017 and March 31, 2018.

Potential Adverse Consequences of Inter Vivos Transfers

Some adverse tax effects and other protections also might occur by transferring the property during a grantor's lifetime to a revocable trust. A brief list of examples is as follows:

- If S Corporation stock is transferred to a revocable trust during a grantor's lifetime, no S election is needed as such trust is typically a grantor trust. However, unless certain elections are timely filed, such transfer could bust the S Corporation election upon the grantor's passing or subject to the grantor to punitive penalties in the shareholder agreement.
- Certain exemptions and protections provided under local law (such as lower real estate taxes or the homestead exemption) may be lost by a transfer of a primary residence to a revocable trust. This includes the possible loss of creditor protection for a primary residence (i.e. homestead).
- An attempt to transfer an interest in an individual retirement account (IRA) might constitute a taxable disposition subjecting the owner to income tax and penalties.
- If a property with a mortgage is transferred to a revocable trust without approval, the bank may be able to call the loan.

Trusts Used for Tax Reduction

Submitted by Kort D. L. Peterson

Trusts Used for Tax Reduction

By Kort D.L. Peterson

Introduction

At first glance, the topic of trusts used for tax reduction may seem pretty simple – just list several types of trusts, talk about them at a high level and we're finished. As is usually the case, however, it's more complicated than that. There is often more than one tax regime that plays into the decision to use a specific type of trust. A client might want to reduce the impact of the income tax, the gift tax, the estate tax or the generation-skipping transfer tax. In some cases, the client might want to reduce the impact of all of these taxes at once. Additionally, although true tax reduction (in the sense of eliminating some portion of a specific tax liability) may be the ideal outcome, many times the best result is tax deferral, or the transfer of the tax liability from one potential taxpayer to another. It is almost always better to pay taxes later rather than to pay taxes now.

A comprehensive, technical explanation of each of the relevant tax regimes is beyond the scope of these materials. Nonetheless, specific rules will be explained as needed for a clear understanding of the usefulness and characteristics of certain specific types of trusts. The remainder of these materials will explore certain specific types of trusts that you may want to recommend to a client who is seeking to reduce taxes, whether eliminating liability, deferring liability, or shifting liability to a different taxpayer.

A. Charitable Remainder Trusts

A charitable remainder trust (or "CRT") is an irrevocable trust formed by a grantor in order to benefit more than one class of beneficiaries, with the remainder benefitting a charitable beneficiary. There are a wide variety of CRTs, but the basic structure is that a grantor sets up the trust and an income stream is paid to either the grantor or other grantor-designated beneficiaries for a period of years or a measuring lifetime and after the income interest terminates, the remainder benefits charity. CRTs are divided into two (2) categories: CRTs whose income payment is determined as an annuity ("CRATs") and CRTs whose income payment is determined under a "unitrust" method ("CRUTs"). CRTs are exempt from income taxes except to the extent that they have unrelated business taxable income, or UBIT. See I.R.C. § 664(c). This means that contribution of a highly appreciated asset with a low basis will provide great benefit to the grantor, insofar as the grantor would not be subject to income tax on the gain inherent in that asset.

The grantor will also generally receive a charitable deduction for the contribution to the CRT. Calculation of the deduction will vary based on the type of CRT. Your client will receive a deduction equal to the value of the property placed in the CRAT reduced by the present value of the annuity payments. See Treas. Reg. § 1.664-2(c). On the other hand, a contribution to a CRUT will produce a deduction equal to the value of the property contributed less the present value of the unitrust interest for a term of years or the life of the income beneficiary, as appropriate. See Treas. Reg. § 1.664-4. The grantor's deduction will also be limited to a specific percentage of the grantor's AGI depending on the type of charitable entity serving as the remainder beneficiary, the type of property contributed to the CRT and powers in certain parties to change the identity of the charitable remainder beneficiary. See Rev. Rul. 80-38; PLR 9452056; I.R.C. § 170(b)(1)(D).

CRATs are CRTs that provide the grantor – or the grantor-selected income beneficiary – with an income stream tied to a set percentage of the donated assets, based on the assets' value at the time of the creation of the trust, regardless of how much they grow over time.

CRUTs are CRTs that tie the income payment to market value of the trust assets, which is evaluated each year. Thus, the payment amount fluctuates with market fluctuations, but the remainder gift to charity is also potentially protected to a greater extent than in a CRAT.

A Net Income Charitable Remainder Unitrust, or "NICRUT", is a type of CRUT that allows deferral of payments to income beneficiaries if trust income is insufficient – the trustee pays the income beneficiary the lesser of (i) trust net income or (ii) the unitrust amount. NICRUTs ensure that trust principal will not be depleted by payments to the income beneficiary, even though the stream of payments may well be less predictable than those in a traditional CRUT.

A Net Income with Makeup Charitable Remainder Unitrust, or "NIMCRUT", is a NICRUT that provides for a makeup of any deferred/reduced payments to income beneficiaries, and the payments are made at a later date, when the trust receives income to "makeup" the deficiency in payment. A NIMCRUT combines the untapped-principal benefit of a NICRUT, with an increase in payment-stream predictability by including the makeup provision.

B. Qualified Domestic Trusts

A Qualified Domestic Trust, or a "QDOT", is the primary mechanism whereby a decedent can transfer assets to a spouse who is not a U.S. citizen and receive the benefit of the unlimited estate tax marital deduction. Section 2056(d) of the Internal Revenue Code (the "Code") expressly denies a marital deduction to a transfer to a spouse who is not a U.S. citizen, unless such transfer is made via a QDOT. Section 2056A defines a QDOT as any trust if (1) the trust agreement contains certain provisions, (2) the trust meets additional requirements contained in the Treasury Regulations intended to ensure collection of estate tax and (3) the decedent's executor has made an election under Section 2056A that is applicable to the trust. Section 2056A provides that the trust agreement for a QDOT must (A) require that at least one trustee of the trust be an individual citizen of the United States or a domestic corporation, (B) provide that no distribution of principal may be made from the trust unless the domestic trustee has the right to withhold from such distribution the tax imposed by Section 2056A on such distribution.

Consider that a QDOT is not a true tax reduction tool – instead, it is primarily a tax deferral tool, as the marital deduction will defer tax until the second death. In any case, it makes sense to ask your clients about citizenship status, and specifically for tax purposes, failing to find out whether your client's spouse is a citizen is an all-too-easy way for a trust typically eligible for the unlimited marital deduction to be fully included in your client's estate.

C. Qualified Personal Residence Trusts

A qualified personal residence trust (a "QPRT"), is a mechanism for transferring a primary residence or vacation home to your client's beneficiaries at a reduced transfer tax cost while retaining the use and benefit of the property for a specified term of years. The transfer of the property to the QPRT is considered a gift to the remainder beneficiaries, but the amount of the gift is diminished by the value of the grantor's retained interest in the trust. The value of this planning tool to your client will depend heavily on the current 7520 rate, which impacts the calculation of the amount of the gift. Another way to increase the benefit of this type of planning is to create two QPRTs and fund each one with a fractional interest in the underlying property – this can result in a fractional interest discount on the value of the property contributed to each QPRT and thereby further diminish the amount of the gift. You may want to advise your client to give each such QPRT a different duration of grantor benefit – as discussed later, this can serve as a hedge against the risk of estate inclusion in the event that the grantor does not survive the term of the QPRT.

At the end of the term of the grantor's benefit, the grantor must either cease occupying the residence or begin paying rent for such use. This illustrates the fact that a transfer to a QPRT is just that – a transfer – and the grantor no longer owns the asset. However, where a client has a beach house with great appreciation potential and knows that she wants to give the house to her children, it may make sense to use a QPRT (or two) to reduce the use of her lifetime exemption amount in the context of the transfer of the beach house.

A QPRT generally cannot own any assets other than the primary residence of the term holder (typically, though not always, the grantor), one other personal residence of the term holder, or a fractional interest therein. See Treas. Reg. § 25.2702-5(b)(2).

The same grantor may not hold a term interest in more than two (2) QPRTs. See Treas. Reg. § 25.2702-5(a)(1). QPRTs that hold fractional interests in the same residence are counted as one trust for this purpose. See id.

The residence must be primarily used as residence of the term holder during the term. See Treas. Reg. § 25.2702-5(c)(2)(iii). This means, among other things, that the residence cannot be used as a hotel or bed and breakfast during the term and qualify as a personal residence for purposes of being treated as a QPRT.

A QPRT is a "grantor" trust for income tax purposes – the grantor is treated as the owner of the trust assets for income tax purposes because the grantor retains the benefit of trust assets for a period of time. See I.R.C. § 677.

Consider that full value of the property will be included in the estate of the grantor if the grantor dies during the term of the trust. See I.R.C. § 2036(a)(1).

D. Defective Trusts

Defective trusts, or more properly, intentionally defective grantor trusts ("IDGTs"), should not cause you to think about calling your malpractice carrier. They acquired the name because when the grantor trust rules in Subchapter J of the Code were first implemented, they were designed to prevent practitioners from avoiding income tax by assigning income to a trust (which then had a lower income tax rate). As time went on and rules evolved, practitioners began to see the advantage of having trust assets that were deemed to be owned by the grantor for income tax purposes – most notably, the ability of assets to grow income tax-free as the grantor paid the income tax on the trust assets, even though they were outside of the grantor's estate for estate tax purposes. Thus, practitioners began intentionally setting up trusts in such a way as to trigger grantor trust status for income tax purposes – so-called "defective" trusts in light of the fact that the trusts did not "work" in light of the initial policy that produced Subchapter J.

IDGTs are more fully discussed later in our materials, so this segment will not discuss the technical requirements for creating an IDGT. Instead, in this segment, we will focus on the potential for tax reduction in connection with the use of IDGTs.

The first potential planning benefit from the use of IDGTs has already been generally referenced – the tax-free growth of trust assets. The trustee of an IDGT does not have to pay income tax on the income generated by the trust assets. Instead, the grantor takes the IDGTs items of income and deduction and credit into account on his personal income tax return. See I.R.C. § 671; Treas. Reg. § 1.671-2(d). Under Section 678 of the Code, a person other than the grantor may be treated as the owner of part or all of a defective trust's assets for income tax purposes, but this type of trust, while "defective", is not an IDGT – when the trust assets are treated as owned by a trust beneficiary, the trust is typically referred to as a "Beneficiary Defective Irrevocable Trust," or BDIT. In either case, the deemed owner of the trust assets pays the income tax on the trust assets, not the trust. This allows trust assets to grow income tax-free. Because of differences between the estate tax rules and the income tax rules, the assets of an IDGT can be treated as owned by the grantor for income tax purposes, but not for estate tax purposes. It almost goes without saying that income tax-free growth outside the client's estate is an exceptionally valuable estate planning tool. Consider further that the payment of the income taxes attributable to the IDGT assets is not considered a gift (even though it effectively increases the value of what is being transferred to the client's beneficiaries when you consider that absent IDGT status, the trust assets would be depleted by payment of income taxes). Thus, the grantor can further diminish his estate by payment of the income taxes without using up any of his lifetime exemption amount. IDGTs can contain provisions that permit the reimbursement of the grantor for taxes paid on income generated by the trust, though this will diminish the benefit of tax-free growth. Even if the reimbursement option is never used, it should be included in the trust agreement for an IDGT in order to give the grantor sufficient flexibility to adapt to changing cash flow needs.

Tax deferral or reduction can also be achieved when the grantor enters into a transaction with the IDGT wherein the grantor sells assets to the IDGT. Because the grantor is treated as the owner of the IDGT assets, a sale of assets from the grantor to the IDGT is not an income tax recognition event. Consequently, if the grantor owns stock in a company with a low basis, he can sell it to his IDGT without recognizing the gain inherent in that stock as income.

E. Education Trusts for Children and Grandchildren

Paying education expenses for children and grandchildren is a very common way clients benefit their descendants. Section 2503 of the Code provides a very favorable exclusion from gift tax for tuition payments paid directly to an educational institution (this exclusion is also applicable to certain payments made for medical expenses). See I.R.C. § 2503(e). Such a payment will not use up lifetime exemption and will not even use up the annual exclusion amount applicable to each such beneficiary. Trusts established to pay for the education expenses of a beneficiary, however, will typically not qualify for the Section 2503(e) exclusion. Thus, while a client can set up a trust for education of his children and grandchildren, he will have to use the annual exclusion and his lifetime exemption to protect such a trust from transfer tax exposure. Remember that direct payments to educational institutions (and healthcare providers) are more tax efficient than a typical trust and may be less expensive for the client.

Health and education exclusion trusts (or "HEETs") may provide for a transfer tax-free way of benefiting children and more remote beneficiaries. A HEET must have a charitable beneficiary with a substantial present economic interest in the trust, but is not subject to gift or GST Tax.

HEETs have been targeted in the Obama administration's most recent greenbook, because they don't want a trustee to be able to make these distributions – the administration would prefer to only give the exclusion to transfers direct from donor. Thus, HEETs may be an aggressive planning tool at this time, but may still be worth exploring for a client who has used up his exemptions but still wants to provide educational benefits for generations of descendants.

F. Generation Skipping Trusts

As discussed above, IDGTs can offer great potential for tax reduction in the estate tax and the income tax regime (at least insofar as trust assets can grow income tax free when the grantor is paying the income tax on trust assets). There is, however, a third layer of tax to consider when drafting a trust – the generation-skipping transfer tax. Congress, in its infinite wisdom, essentially looked at the estate tax back in the 1980s and said, "well, this is great, but if a grandmother decides to give assets to her grandchild, we're missing out on a layer of estate tax at the mother/daughter level." This thought process prompted them to implement the generation-skipping transfer tax (the "GST Tax") in 1986. The GST Tax assigns a donor and the donor's beneficiaries to specific generations in relation to each other and imposes a tax on transfers that "skip" a generation. This includes direct donative transfers (a "direct skip"), a generation-skipping trust distribution during the term of such trust (a "taxable distribution"), or a generation-skipping trust distribution in the context of the termination of a trust (a "taxable termination"). As with the estate and gift taxes, each taxpayer has a GST exemption amount that can be allocated to skip transfers during lifetime (with respect to certain skip transfers) or at death on the IRS Form 706 federal estate tax return (with respect to other types of transfers).

Drafting a generation-skipping trust from a tax reduction standpoint pulls in several different kinds of tax at once. GST Tax is, of course, a motivator, but estate tax and income tax are also relevant. In fact, it often makes sense for generation-skipping trusts to be IDGTs, in order to permit income tax-free growth of trust assets. The potential duration of the generation-skipping trust is an important issue to discuss with your client. In state of Georgia, we have a “wait-and-see”-style rule against perpetuities which limits the duration of a Georgia trust to a maximum of the longer of 90 years or a life in being plus 21 years. It may be that your client’s estate planning goals would be better served by selecting a different jurisdiction with a more generous rule against perpetuities to stretch the number of generations who may benefit from trust assets without subjecting same to estate or GST Tax. South Dakota, for instance, has modified its law to permit trusts of unlimited duration. Delaware, Alaska, Colorado and other states also have more generous rules than Georgia, although some of these states treat real property differently from other asset types.

G. Funding the Trust

Funding a trust implemented for tax reduction purposes can carry significant tax consequences if not carried out properly. For example, if an IDGT is funded by one grantor and then another grantor subsequently contributes, it may be that the grantor trust status will be changed by the subsequent contribution – it is possible that a trust will be considered a grantor trust as to only a portion, but not all, of the trust assets and it is possible that part of a trust could be treated as owned by one donor for income tax purposes and another portion of the same trust could be treated as owned by separate donor for income tax purposes. See I.R.C. § 671; Treas. Reg. § 1.671-2.

Grantor Trusts

Submitted by Bland Byrne

Grantor Trusts

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I. Statutory Background

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   b. Regulation Section 1.671-2(e): Who Is The Grantor?
   c. IRC 672: Definitions and Rules
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   g. IRC 676: Power to Revoke
   h. IRC 677: Income for Benefit of Grantor
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II. Specific Types of Grantor Trusts

   a. Revocable (Living) Trusts
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III. Tax Returns

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e. Exceptions Applicable to All Optional Methods

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Attachments: Sample Forms (Courtesy of SunTrust Bank)

Irrevocable Life Insurance Trust

Grantor Retained Annuity Trust

Grantor Trusts

Although trusts are creatures of state law, Grantor Trusts are entirely a federal income tax law concept. With the advent of a graduated income tax, it became expedient for taxpayers to find ways to split their income into several parts, each of which would have a lower marginal rate than would the entire income together. One possibility was to split a taxpayer's income among several trusts controlled by and for the benefit of the taxpayer. The Grantor Trust rules of IRC 671 through 679 are one answer to this strategy. The Grantor Trust rules tax the income of a trust directly to a taxpayer, usually but not always the Grantor of the trust, as though the trust did not exist.

I. Statutory Background

a. IRC 671: Trust Income, Deductions, and Credits Attributable to Grantors and Others as Substantial Owners

IRC Section 671 specifies an exception to the general rule that trusts are separately taxed on their own income. If a person, usually but not always the grantor of the trust, is treated as the owner of the trust under any provision of Sections 672 through 679, then all items of income, deduction and credits are treated as belonging directly to the grantor (or other person, as the case may be).

Note that Sections 671 through 679 do not provide for a flow-through scheme of taxation as in the case of partnerships and Subchapter S Corporations. The rules for those other entities have provisions for what tax items flow through to owners and how, but the Grantor Trust Provisions of Sections 671 through 679 simply treat the tax items as belonging to the owner. As a result, there is no such thing as a Grantor Trust Income Tax Return Form. (See below for methods of reporting income from Grantor Trusts.)

Note also that Section 671 may apply to only part of a trust, in which case that part of the trust is treated as if it were a stand-alone Grantor Trust, and the remaining part is treated as a stand-alone trust subject to the ordinary rules of trust taxation.

b. Regulation Section 1.671-2(e): Who Is The Grantor?

"Grantor" is a broad term. It includes any person to the extent such person either creates a trust, or directly or indirectly makes a gratuitous transfer of property to a trust. If a person creates or funds a trust on behalf of another person, both persons are treated as Grantors, although a person who creates a trust but makes no gratuitous transfers to the trust is not treated as an owner of any portion of the trust under IRC 677 or 679. Also, a person who funds a trust with an amount that is directly reimbursed to such person within a reasonable time and who makes no other gratuitous transfers to the trust is not treated as an owner under IRC 677 or 679.

Grantor also includes any person who acquires an interest in a trust from a grantor if the interest is an interest in certain investment trusts, liquidating trusts, or environmental remediation trusts.

If a gratuitous transfer is made by a corporation or partnership for a business purpose of the corporation or partnership, then the corporation or partnership will ordinarily be treated as the Grantor. But if the gratuitous transfer is not for a business purpose of the corporation or partnership, but rather for the personal purposes of one or more of the shareholders or partners, then the gratuitous transfer will be treated as a a constructive distribution to such shareholders or partners, and such shareholders or partners will be treated as the Grantors.

If a trust makes a gratuitous transfer to another trust, the Grantor of the transferor trust will generally be treated as the Grantor of the transferee trust. However, if a person with a general power of appointment over the transferor trust exercises that power in favor of another trust, then such person will be treated as the grantor of the transferee trust, even if the Grantor of the transferor trust is someone else.

c. IRC 672: Definitions and Rules

IRC Section 672 contains definitions and rules for the operation of Sections 673 through 679.

Four defined terms are important to the Grantor Trust rules:

An **Adverse Party** is a person who has a substantial beneficial interest in the trust which would be adversely affected by the exercise or nonexercise of the power which the person possesses respecting the trust. A general power of appointment is defined to be a beneficial interest. IRC 672(a)

A **Nonadverse Party** is a person who is not an Adverse Party. IRC 672(b)

A **Related of Subordinate Party** is a nonadverse party who is one of the following: the grantor's spouse if living with the grantor; the grantor's father, mother, issue, brother or sister; an employee of the grantor; a corporation or any employee of a corporation in which the stock holdings of the grantor and the trust are significant from the viewpoint of voting control; a subordinate employee of a corporation in which the grantor is an executive. IRC 672(c)

For purposes of Sections 672(f), 674, and 675, a Related of Subordinate Party is presumed to be **subservient** to the grantor in respect to powers granted such person, unless shown not to be subservient by a preponderance of the evidence. IRC 672

The application of the Grantor Trust Rules is subject to certain general rules:

A person is considered to have a power described in Sections 671 through 679 even though the exercise of the power is subject to giving notice or takes effect only on the expiration of a certain amount of time after exercise. IRC 672(d)

The grantor is treated as holding any power or interest of the grantor's spouse, either a spouse at the time of the creation of the power or interest or a person who later becomes the grantor's spouse, though in the latter case, only after the person becomes the grantor's spouse. IRC 672(e)

Subject to certain terms and conditions beyond the scope of this paper, the Grantor Trust Rules apply only to the extent that such application results in an amount being taken into account in computing the income of a citizen or resident of the United States or a domestic corporation. IRC 672(f)

d. IRC 673: Reversionary Interests

A grantor is treated as the owner of any portion of a trust in which the grantor has a reversionary interest in corpus or income exceeding 5% of the value of such portion as of the inception of such portion. IRC 673(a)

An exception to the rule of Section 673(a) is a reversionary interest taking effect at the death of a lineal descendant of the grantor who holds all the present interests of a portion of the trust, if such beneficiary dies before age 21. IRC 673(b)

The value of a reversionary interest is determined assuming the maximum exercise of discretion in favor of the grantor. IRC 673(c)

If the date for reversion is postponed, the postponement is treated as a new transfer. However, income is not included in the income of the grantor by reason of this rule if such income would not be includible in the absence of the postponement. IRC 673(d)

e. IRC 674: Power to Control Beneficial Enjoyment

The grantor is treated as the owner of any portion of a trust in which the beneficial enjoyment of the corpus of income is subject to a power of disposition exercisable by the grantor or a nonadverse party, or both, without the approval of consent of any adverse party. IRC 674(a)

There are twelve exceptions to the general rule of Section 674(a).

Section 674(a) does not apply to the following powers, regardless of by whom held:

i. A power to apply income to support a dependent, to the extent the power would not be subject to tax under Section 677(b). IRC 674(b)(1)

ii. A power affecting beneficial enjoyment only after occurrence of an event such that the grantor would not be treated as the owner under Section 673 if the power were a reversionary interest, but the grantor may be treated as the owner after the occurrence of the event unless the power is relinquished. IRC 674(b)(2)

iii. A power exercisable only by will, other than a power to appoint accumulated income where the income is accumulated in the discretion of the grantor or a nonadverse party or both, without the approval or consent of an adverse party. IRC 674(b)(3)

iv. A power to allocate enjoyment of corpus or income if corpus or income is irrevocably payable for a charitable purpose or to an employee stock ownership plan in a qualified gratuitous transfer. IRC 674(b)(4)

v. A power to distribute corpus to or for beneficiaries or a class of beneficiaries (whether or not income beneficiaries) provided that the power is limited by a reasonably definite standard set forth in the trust instrument, and provided that no one has a power to add to the beneficiaries or class of beneficiaries except to add after-born or after-adopted children. IRC 674(b)(5)(A)

vi. A power to distribute corpus to or for a current income beneficiary, provided that the distribution of corpus must be chargeable against the proportionate share of corpus held in trust for the payment of income to the beneficiary as if the corpus constituted a separate trust, and provided that no one has a power to add to the beneficiaries or class of beneficiaries except to add after-born or after-adopted children. IRC 674(b)(5)(B)

vii. A power to withhold income temporarily provided that any accumulated income must ultimately be payable to the beneficiary from whom distribution was withheld or to his estate or appointees or alternate takers in default of appointment, or on termination of the trust or in conjunction with a distribution of corpus which is augmented by accumulated income to the current income beneficiaries in shares which have been irrevocably specified in the trust instrument. This exception has additional requirements related to powers of appointment, conditions based on the beneficiary's survival, and powers to add beneficiaries. IRC 674(b)(6)

viii. A power to withhold income during the beneficiary's disability or while the beneficiary is less than 21, provided that no one has a power to add to the beneficiaries or class of beneficiaries except to add after-born or after-adopted children. IRC 674(b)(7)

ix. A power to allocate receipts and disbursements between corpus and income, even though expressed in broad language. IRC 674(b)(8)

x. A power solely exercisable by trustees none of whom is the grantor (or spouse of the grantor), and no more than half of whom are related or subordinate parties who are subservient to the grantor, to distribute, apportion, or accumulate income to or for beneficiaries or within a class of beneficiaries, provided that no one has a power to add to the beneficiaries or class of beneficiaries except to add after-born or after-adopted children. IRC 674(c)(1)

xi. A power solely exercisable by trustees none of whom is the grantor (or spouse of the grantor), and no more than half of whom are related or subordinate parties who are subservient to the grantor, to pay out corpus to or for beneficiaries or within a class of beneficiaries (whether or not income beneficiaries), provided that no one has a power to add to the beneficiaries or class of beneficiaries except to add after-born or after-adopted children. IRC 674(c)(2)

xii. A power solely exercisable by trustees none of whom is the grantor (or spouse of the grantor living with the grantor), to distribute, apportion, or accumulate income to or for beneficiaries or within a class of beneficiaries, whether or not the conditions of Section 674(b)(6) or (7) are satisfied, if such power is limited by a reasonably definite external standard which is set forth in the trust instrument, provided that no one has a power to add to the beneficiaries or class of beneficiaries except to add after-born or after-adopted children. IRC 674(d)

f. IRC 675: Administrative Powers

A grantor is treated as the owner of any portion of a trust in respect of which:

i. The grantor or a nonadverse party, or both, without the approval of any adverse party, has a power enabling the grantor or any person to purchase, exchange, or otherwise deal with the corpus or income for less than adequate consideration. IRC 675(1)

ii. The grantor or a nonadverse party, or both, has a power enabling the grantor to borrow corpus or income, directly or indirectly, without adequate interest or security, except where a trustee (other than the grantor) is authorized under a general lending power to make loans to any person without regard to interest or security. IRC 675(2)

iii. The grantor (or grantor's spouse) has directly or indirectly borrowed the corpus or income and has not completely repaid the loan, including any interest, before the beginning of the taxable year. The preceding sentence does not apply to a loan which provides for adequate interest and adequate security, if such loan is made by a trustee other than the grantor and other than a related or subordinate trustee subservient to the grantor. IRC 675(3)

iv. A power of administration is exercisable in a nonfiduciary capacity by any person without the approval of any person in a fiduciary capacity. A **power of administration** is one of the following powers: i) a power to vote or direct the voting of stock or securities of a corporation in which the holdings of the grantor and the trust are significant from the viewpoint of voting control; ii) a power to control the investment of the trust funds either by directing investments or by vetoing investments, to the extent that the trust funds consist of stocks or securities of corporations in which the holdings of the grantor and the trust are significant from the viewpoint of voting control; or

iii) a power to reacquire the trust corpus by substituting other property of an equivalent value. IRC 675(4)

g. IRC 676: Power to Revoke

The grantor is treated as the owner of any portion of a trust when at any time the power to revest in the grantor title to such portion is exercisable by the grantor or a nonadverse party, or both. IRC 676(a)

This rule does not apply when the power can only affect beneficial enjoyment of income for a period beginning after the occurrence of an event such that the grantor would not be treated under IRC 673 as the owner if the power were a reversionary interest, but the grantor may be treated as the owner after the occurrence of such event unless the power is relinquished. IRC 676(b)

h. IRC 677: Income for Benefit of Grantor

The Grantor is treated as the owner of any portion of a trust whose income, without the approval of an Adverse Party is, or in the discretion of the Grantor or an Adverse Party, or both, may be

i. distributed to the Grantor or the Grantor's spouse;

ii. accumulated for future distribution to the Grantor or the Grantor's spouse; or

iii. applied to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse (except policies irrevocably payable for charitable purposes).

This rule does not apply when the power can only affect beneficial enjoyment of income for a period beginning after the occurrence of an event such that the Grantor would not be treated under IRC 673 as the owner if the power were a reversionary interest, but the grantor may be treated as the owner after the occurrence of such event unless the power is relinquished. IRC 677(a)

Income of a trust is not taxable to the Grantor under Section 677(a) **or any other income tax provision** merely because such income in the discretion of another person, the trustee, or the Grantor acting as trustee or co-trustee, may be applied or distributed for the support or maintenance of a beneficiary (other than the Grantor's spouse) whom the Grantor is legally obligated to support, except to the extent such income is so applied or distributed. IRC 677(b)

i. IRC 678: Person Other Than Grantor Treated As Substantial Owner

A person other than the grantor is treated as the owner of any portion of a trust with respect to which such person has a power exercisable solely by himself to vest corpus or income in himself, or such person has partially released or otherwise modified such a power and afterwards retains such control as would subject a Grantor of a trust to treatment as the owner under Sections 671 through 677. IRC 678(a)

Section 678(a) does not apply with respect to a power over income if the Grantor of the trust or a transferor to whom Section 679 applies is otherwise treated as the owner of the trust. IRC 678(b)

Section 678(a) also does not apply to a power which enables the holder of the power, acting as trustee or co-trustee, merely to apply income for the support or maintenance of a person whom the holder is legally obligated to support, except to the extent such income is so applied. IRC 678(c)

Section 678(a) also does not apply with respect to a power which has been renounced within a reasonable time after the holder first became aware of its existence. IRC 678(d)

j. IRC 679: Foreign Trusts With U. S. Beneficiaries

The general rule of IRC 679 is that a United States Person (defined in IRC 7701(a)(30)) who directly or indirectly transfers property to a foreign trust is treated as the owner for his taxable year of the portion of such trust attributable to such property if for such year there is a United States beneficiary of any portion of such trust. The exceptions and special rules relating to this section are beyond the scope of this paper. IRC 679

II. Specific Types of Grantor Trusts

a. Revocable (Living) Trusts

Revocable Trusts can be used for many purposes, but are often used as substitutes or supplements for other documents such as powers of attorney for disability planning or wills for estate planning.

b. Life Insurance Trusts

Life Insurance Trusts are irrevocable trusts designed to remove the proceeds of life insurance on the life of the Grantor or the Grantor and Grantor's spouse from their taxable estates. They are Grantor Trusts pursuant to IRC 677(a)(3) because the trust income and corpus may be used to pay premiums on policies of life insurance on the life of the Grantor or the Grantor's spouse. However, Life Insurance Trusts usually are not funded with income producing assets, so there is no income to be taxed.

The successful operation of a Life Insurance Trust depends upon estate tax rules on when proceeds of life insurance are part of the gross estate, and upon case law relating to taxable gifts.

Proceeds of life insurance on the life of a decedent are included in the gross estate if paid to the estate or if the decedent possessed at death any incidents of ownership, exercisable alone or in conjunction with any other person. (IRC 2042) Incidents of ownership refer to the right of the insured or his estate to the economic benefits of the policy, and include the power to change the beneficiary, to surrender or cancel the policy, to assign the policy, to revoke an assignment, or to pledge the policy for a loan. There is not an exclusive list of incidents of ownership, and in some cases, incidents of ownership held by a corporation may be attributed to the decedent because of stock ownership. Regulation (Section 20.2042-1(c)) Thus, all incidents of ownership must belong to the trust and not the Grantor. Even so, if the policy is assigned with all incidents of ownership to the trust within three years of the death of the Grantor, the proceeds will be included in the Grantor's gross estate pursuant to IRC 2035. Therefore, if possible, it is preferable to have the trust purchase a new policy rather than assigning an existing policy to it.

To avoid taxable income pursuant to IRC 677(a)(3), money is usually advanced by the Grantor to the trust to pay the premiums as they come due. Such advances are taxable gifts and ordinarily the gift tax exclusion of IRC 2503(b) would not be available, because a gift to pay premiums for life insurance is a gift of a future interest. However, the case of Crummey v. Commissioner, 397 F.2d 82 (9th Cir.) held that transfers in trust which would otherwise be gifts of future interests are considered gifts of present interests qualifying for the gift tax exclusion of IRC 2503(b). This is true even though the withdrawal right lapses if not exercised and even though withdrawal rights are granted to minors for whom no guardian has been appointed. Rev. Rul. 73-405 If the premiums are less than the gift tax exclusion, then the Grantor can fund the premiums without using any of the Grantor's unified credit. If the premiums are greater than the gift tax exclusion for one beneficiary, the trust may provide for multiple withdrawal powers so that the combined exclusions will cover the premiums. However, the lapse of withdrawal powers is a release of a power of appointment under IRC 2514(e), so that the beneficiaries may be treated as making gifts to each other as their powers lapse. This problem can be addressed by not using the full gift tax exclusion for each withdrawal right, but rather limiting the withdrawal right to a $5,000 or 5% of value withdrawal right (but no greater than the gift tax exclusion), which is not treated as a release of a power of appointment under IRC 2514(e).

During the life of the Grantor (or the lives of the Grantor and the Grantor's spouse if a joint life insurance policy is used), a Life Insurance Trust ordinarily would do nothing besides hold insurance policies and pay premiums. At the death of the insured(s), however, the trust would receive the insurance proceeds, and handle them in accordance with the trust document. The intent of the arrangement might be simply to provide an inheritance for heirs and distribute the proceeds immediately, or it might manage the funds for future generations. Life Insurance Trusts have often been used to provide liquidity for taxable estates by, for example, purchasing illiquid assets such as closely held businesses from the decedent's estate.

c. Rabbi Trusts

A Rabbi Trust gets its name from the fact that the arrangement was first used by a congregation to provide for the retirement of its rabbi. A Rabbi Trust is a deferred compensation arrangement for employees utilizing a grantor trust. Ordinarily an employee is taxed on deferred compensation received under an unfunded non-qualified deferred compensation plan when the payments are made available to him, under the theory of constructive receipt (IRC 451) or economic benefit (IRC 61). In order not to be taxed under the constructive receipt theory, amounts may neither be received or set aside for the employee. Crediting amounts to the account of an employee does not come within the theory if the availability is subject to substantial limitations. In order not to be taxed under the economic benefit theory, funds set aside for an employee may not be protected from the employer's creditors. In a Rabbi Trust arrangement, the employer funds an irrevocable trust but retains administrative powers. The funds may only be used to pay benefits to employees, but the assets remain available to creditors of the employer. A Rabbi Trust has the advantages of creating a fund for the employees but being treated as unfunded for tax purposes, and so avoiding the limitations of qualified retirement plans, such as nondiscrimination requirements. It has the disadvantages of having its income taxed to the employer under the Grantor Trust rules, and having its corpus potentially subject to claims of creditors.

Rev. Proc. 92-64 provides a model trust form to serve as a safe harbor for Rabbi Trusts.

d. Qualified Subchapter S Trusts (QSST)

A Subchapter S corporation differs from other corporations in that it does not report and pay taxes as a separate entity. Rather it passes its income and losses, and items thereof, through to its shareholders pursuant to rules contained in Subchapter S (IRC Sections 1361 through 1379). The rules are numerous, but among them is a requirement that all shareholders must be individuals, with only a few exceptions. IRC 1361(b)(1)(B). Among the exceptions are certain trusts described in IRC 1361(c)(2), three of which are Grantor Trusts.

The first is a Grantor Trust all of which is treated under the Grantor Trust rules as owned by an individual who is a citizen or resident of the United States. IRC 1361(c)(2)(A)(i)

The second is actually a former Grantor Trust, one which was described in the previous paragraph, but for the two year period beginning the day of the deemed owner's death. IRC 1361(c)(2)(A)(ii)

The third exception for Grantor Trusts is a Qualified Subchapter S Trust (QSST) described in IRC 1361(d). A trust meeting the requirements of IRC 1361(d) is treated as a trust described in the first exception, above. IRC 1361(d)(1)(A)

A QSST can have only one income beneficiary during the life of the beneficiary. Any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary. The income interest of the current income beneficiary must terminate on the earlier of the beneficiary's death of the termination of the trust. Upon the termination of the trust or the death of the beneficiary, the trust must distribute all of its assets to such beneficiary. And all of the income which is distributed or required to be distributed currently must be distributed to one individual who is a citizen or resident of the United States. A substantially separate and independent share of a trust is treated as a separate trust. IRC 1361(d)(3)(A)

A trust is not a QSST unless the beneficiary (or the beneficiary's legal representative) makes an election with respect to each corporation the stock of which is held by the trust. The election cannot be revoked without consent of the Secretary. IRC 1361(d)(2)

e. Intentionally Defective Grantor Trusts

An Intentionally Defective Grantor Trust (IDGT) takes advantage of the differences between income tax rules and estate and gift tax rules. Numerous provisions define when a gift is complete for gift tax purposes and when an asset is included in a decedent's taxable estate. (With respect to gift tax, see for example IRC 2511 through 2519; with respect to estate tax, see for example IRC 2031 through 2046.) These rules do not match seamlessly with the Grantor Trust rules of IRC 671 through 679, so that it is possible to transfer assets into a Grantor Trust in a way which is subject to gift tax, removing the asset from the Grantor's future taxable estate, even though for income tax purposes, the Grantor is still considered the owner of the asset. A high net worth individual might want to use an IDGT in order to minimize the amount of gift tax on gifts. This strategy works because the amount of income tax paid by the Grantor is essentially an additional gift to the beneficiaries of the trust, but no gift tax is due on it.

A further refinement on this strategy is an installment sale by the Grantor to the IDGT. (The trust should be funded with sufficient assets to be able to make payments on the installment note to the Grantor, generally at least 10% of the total transfer value.) There is no capital gains tax due on the installment sale to the trust because the Grantor is treated as essentially selling the asset to himself for income tax purposes. For the same reason, no income tax is due with respect to the interest paid to the Grantor on the installment note. To the extent that the growth rate on the assets sold to the IDGT is greater than the interest rate on the installment note taken back by the Grantor, the excess is passed on to the trust beneficiaries free of any gift, estate or GST tax.

A lot can go wrong with an IDGT strategy, so it is not for everyone. First of all, it is only useful for taxpayers subject to the estate tax, which is not many. Second, beyond the estate tax threshold, the taxpayer must be confident of always having enough money to pay the income tax on the trust income, no matter how successful the assets in the trust turn out to be, and no matter how unsuccessful the Grantor's other assets turn out to be, because the trust is irrevocable. And finally, although gift and estate tax rules are different from the Grantor Trust rules, there is a lot of overlap, so that a power or interest which makes the trust a Grantor Trust may also make it part of the Grantor's taxable estate. The drafter must be very careful to pick a power or interest that falls in the crack between gift and estate tax rules and Grantor Trust rules. Possibilities include the power to substitute property of equivalent value (IRC 674(a); Jordahl, 65 TC 92 (1975)); or a power in a nonadverse party to add beneficiaries (Madorin, 84 TC 677 (1985), though this case is solely an income tax case). Other possibilities might be authorizing the trustee to distribute income for the benefit of the Grantor's spouse without the consent of an adverse party (IRC 677(a)(1); or giving a related party the power to sprinkle income or corpus not limited to a reasonably definite external standard (IRC 674 and 672(c)). Be careful of the possible interplay of various provisions of the trust instrument.

f. Qualified Personal Residence Trusts

A Qualified Personal Residence Trust (QPRT) is a method of getting a valuation discount when transferring a personal residence. The Grantor transfers his or her personal residence to an irrevocable trust but retains the right to live in the residence for a certain period of time. The retained right to live in the residence makes the trust a Grantor Trust pursuant to IRC 677. Upon the expiration of the term, the residence is typically transferred to the Grantor's children or held in trust for them. Upon the expiration of the term, the Grantor may no longer live in the residence without paying a fair market rent.

If the Grantor dies before the end of the term, then pursuant to IRC 2036 the value of the residence is included in the Grantor's taxable estate, but if the Grantor survives the term, then the residence is not in the Grantor's taxable estate.

A gift occurs when the residence is transferred to the QPRT. Normally, the retained interest of the Grantor would be disregarded when valuing the gift, pursuant to IRC 2702, so that the value of the gift would be the full fair market value of the residence. However, a QPRT is an exception to the rule, so that the Grantor is allowed to reduce the value of the gift by the present value of the retained interest to live in the residence. IRC 2702(a)(3)(A)(ii)

Detailed requirements for a QPRT are contained in Regulation Section 25.2702-5.

A QPRT may be converted to a Grantor Retained Annuity Trust upon the sale of the residence. Regulation Section 25.2702-5(c)(8)

g. Grantor Retained Annuity Trusts

A Grantor Retained Annuity Trust (GRAT) is another exception to IRC 2702 which allows a Grantor to obtain a valuation discount for a gift as a result of a retained interest and also to remove the assets from the Grantor's estate. It is an irrevocable trust which pays the Grantor a fixed amount annuity no less often than annually for a term of years. If the fixed amount is a stated dollar amount, the trust is a Grantor Retained Annuity Trust. The stated dollar amount cannot exceed 120 percent of the stated dollar amount payable in the preceding year. If the fixed amount is a fixed fraction of the initial fair market value of the property transferred to the trust, the trust is a Grantor Retained Unitrust. An annuity interest does not fail to be a qualified annuity interest merely because the trust permits income in excess of the amount required to pay the annuity amount to be paid to the holder of the annuity interest, but such a right to receive excess income is not taken into account in valuing the annuity interest. A right of withdrawal, whether or not cumulative, is not a qualified annuity interest.

If the Grantor dies before the end of the term, then pursuant to IRC 2036 the value of the trust assets are included in the Grantor's taxable estate, but if the Grantor survives the term, then they are not.

A gift occurs when the assets are transferred to the GRAT. Normally, the retained interest of the Grantor would be disregarded when valuing the gift, pursuant to IRC 2702, so that the value of the gift would be the full fair market value of the assets. However, a GRAT is an exception to the rule, so that the Grantor is allowed to reduce the value of the gift by the present value of the retained interest to live in the residence. IRC 2702(a)(2)(B), 2702(b)

Detailed requirements for a GRAT are contained in Regulation Section 25.2702-3.

h. Grantor Retained Unitrusts

A Grantor Retained Unitrust (GRUT) is governed by the same provisions as a GRAT, but instead of paying a stated dollar amount to the grantor each year for a term of years, a GRUT pays a fixed fraction of the net fair market value of the trust assets, determined annually, payable periodically but not less frequently than annually, but only to the extent the fraction or percentage does not exceed 120% of the fixed fraction payable in the preceding year.

As with a GRAT, if the Grantor dies before the end of the term, then pursuant to IRC 2036 the value of the trust assets are included in the Grantor's taxable estate, but if the Grantor survives the term, then they are not.

A gift occurs when the assets are transferred to the GRUT. Normally, the retained interest of the Grantor would be disregarded when valuing the gift, pursuant to IRC 2702, so that the value of the gift would be the full fair market value of the assets. However, a GRUT is an exception to the rule, so that the Grantor is allowed to reduce the value of the gift by the present value of the retained interest to live in the residence. IRC 2702(a)(2)(B), 2702(b)

Detailed requirements for a GRUT are contained in Regulation Section 25.2702-3.

III. Tax Returns

There are four methods for reporting the taxes of a Grantor Trust. 2014 Instructions for Form 1041; Regulations Section 1.671-4

a. General Rule (1041 filed)

The general rule requires filing an income tax return for the trust on Form 1041. However, only the entity information section of Form 1041 needs to be completed; no dollar amounts are filled in. Income, deductions and credits are reported on an attachment (there is no official form for the attachment) in the same detail it would be reported on the tax return of the person to whom it is taxable. The attachment must also include the name, address and tax identification number of the person to whom the income is taxable. The trustee must give the Grantor or other person to whom the income is taxable a copy of the attachment.

If only part of the trust is a Grantor Trust, the income, deductions and credits for the non-Grantor part is reported normally on the same Form 1041.

b. Optional Method 1 (1041 not filed)

Optional Method 1 is only available if the trust is treated as owned by just one Grantor or other person; however, spouses are treated as one person if they file jointly. Under this method, no tax return is filed by the trust. The trustee must give all payers of income during the year the name and TIN of the Grantor or other person treated as the owner of the trust, and the address of the trust. The person treated as owner must provide the trustee with a signed Form W-9. Unless the person treated as owner of the trust is a trustee or co-trustee of the trust, the trustee must give the owner a statement that shows all items of income, deduction and credit of the trust, that identifies the payer of each item, that explains how the owner is to take those items into account when figuring the person's tax, and that informs the owner that those items must be included when figuring the owner's tax.

Grantor Trusts using Optional Method 1 do not need an EIN for the trust.

c. Optional Method 2 (1041 not filed)

Optional Method 2 is only available if the trust is treated as owned by just one Grantor or other person; however, spouses are treated as one person if they file jointly.

Under this method, no tax return is filed by the trust. The trustee must give all payers of income during the year the name, address and TIN of the trust, and file with the IRS the appropriate Forms 1099 to report the income and gross proceeds paid to the trust during the year that show the trust as payer and the person treated as owner of the trust as payee, reporting each type of income in the aggregate and each item of gross proceeds separately. Unless the person treated as owner of the trust is a trustee or co-trustee of the trust, the trustee must give the owner a statement that shows all items of income, deduction and credit of the trust, that identifies the payer of each item, that explains how the owner is to take those items into account when figuring the person's tax, and that informs the owner that those items must be included when figuring the owner's tax. Giving this statement satisfies the requirement to give the recipient copies of the Forms 1099 filed by the trustee.

d. Optional Method 3 (1041 not filed)

Optional Method 3 is available if the trust is treated as owned by two or more Grantors or other persons. Under this method, no tax return is filed by the trust. The trustee must give all payers of income during the year the name, address and TIN of the trust, and file with the IRS the appropriate Forms 1099 to report the income and gross proceeds paid to the trust during the year attributable to the part of the trust treated as owned by each owner that show the trust as payer and the person treated as an owner as payee, reporting each type of income in the aggregate and each item of gross proceeds separately. The trustee must give each owner a statement that shows all items of income, deduction and credit of the trust attributable to the part of the trust treated as owned by each owner, that identifies the payer of each item, that explains how the owner is to take those items into account when figuring the person's tax, and that informs the owner that those items must be included when figuring the owner's tax. Giving this statement satisfies the requirement to give the recipient copies of the Forms 1099 filed by the trustee.

e. Exceptions Applicable to All Optional Methods

The following trusts cannot report using one of the optional methods: i) a common trust fund, ii) a foreign trust or one that has foreign assets, iii) a Qualified Subchapter S Trust, iv) a trust all of which is treated as owned by a person whose tax year is not the calendar year, iv) a trust which has an owner who is not a U. S. person, and v) a trust which has an owner which is an exempt recipient for information reporting purposes, unless at least one other owner is not exempt and the trustee reports without treating any of the deemed owners as exempt recipients.

f. Changing Filing Methods

Filing methods can be changed. If the general method filing a Form 1041 has been used, then a final Form 1041 must be filed, indicating on the front of the form that it is the final Form 1041 for the Grantor Trust. Detailed requirements for changing reporting methods among the four options are contained in Regulations Section 1.671-4(g).

Grantor Trust Forms

Courtesy of SunTrust Bank

IRREVOCABLE LIFE INSURANCE TRUST FORM

I hereby transfer, assign and convey to the Trustee hereinafter named (the "Trustee"), as Trustee, the sum of Ten Dollars ($10.00), in trust for the beneficiaries to be held, managed and distributed upon the uses and trusts hereinafter set out.

ITEM I

Irrevocable

I have been fully advised and understand and declare that this trust is and shall be irrevocable, and I shall have no right, title or interest in or power, privilege or incident of ownership in regard to any of the property in this trust and no right to alter, amend, modify, revoke or terminate this trust or any of its provisions.

ITEM II

Family

On the date of execution of this agreement, I am married to ___________ ______________, sometimes referred to in this agreement as my "spouse," and my living children are ______________________________, ___________________ and _________________________.

ITEM III

Grantor's Lifetime

(a) **Accumulate Income.** During my lifetime, the Trustee shall hold and manage the trust property and shall accumulate any income received therefrom and add the same to trust principal, except as provided in paragraphs (b) and (c) of this Item.

(b) **No Duty to Invest.** The Trustee shall have no duty to invest the principal of this trust or to make periodic reports to the beneficiaries (other than notifications of withdrawal rights as provided hereinafter) with respect to the principal and income of the trust during my lifetime. Except for giving notifications of withdrawal rights, no Trustee serving hereunder, whether during my lifetime or after my death, shall have any liability, duty or responsibility with respect to the acquisition or maintenance of any insurance policy, including, without limitation, any duty to audit or inquire into the financial condition of any insurance company, to monitor the performance of any insurance policy, to pay premiums, to see that such premiums are paid by me or others, or to notify any persons of the nonpayment of such premiums. The Trustee may, however, apply any dividends received on any insurance policy and may borrow upon the cash value of any policy to pay such premiums, and otherwise may use any income or principal of the trust for such purpose. In addition, the Trustee shall have and may exercise all rights, elections, options, privileges and other powers with respect to the insurance policies in which the trust has an interest, including the right to exercise any conversion privilege or option to purchase additional insurance, the right to apply the cash value of any policy to the purchase of paid-up or extended insurance, and the right to surrender any policy in exchange for the cash value thereof.

(c) **Termination.** Notwithstanding the foregoing provisions of this Item, during my lifetime, the individual Trustee may distribute the trust property, per stirpes, to my descendants who are then living (other than any Trustee hereunder), if the Trustee determines that the original purpose for creating the trust has been accomplished or that it is in the best interests of the beneficiaries hereof to distribute such property and terminate the trust; provided that no distribution shall be made under this paragraph which would discharge or satisfy, in whole or in part, any legal obligation, of support or otherwise, that I or any Trustee hereunder may have.

ITEM IV

After Grantor's Death

(a) **Collection of Death Benefits.** After my death, the Trustee shall collect any property payable to the trust by reason of my death. In collecting any insurance proceeds, the Trustee may elect any optional mode of settlement, and the payment to and the receipt by the Trustee of such proceeds shall be a full discharge of the liability of any insurance company, which company need not take notice of this instrument or see to the application of any payment by the Trustee. The Trustee may institute legal action to enforce payment under any insurance policy, but shall not be required to institute such legal action without indemnification satisfactory to it for any attorneys' fees or other resulting expense.

(b) **Trust Property.** After my death, the Trustee shall deliver to the personal representative of my estate any property paid to the Trustee that is included in my gross estate as finally determined for federal estate tax purposes, and shall hold, manage and distribute the remaining property of this trust, and any additional property received by the Trustee, upon the uses and trusts hereinafter set out.

(c) **Income Distributions.** The Trustee may distribute such part, all or none of the net income, from the property currently to or for the benefit of my spouse and my descendants in such amounts and proportions among them as the Trustee in its sole discretion shall deem best, taking into consideration any other available resources they or any of them may have to the knowledge of the Trustee. Any income not distributed currently shall be accumulated and added to the principal of the trust.

(d) **Principal Distributions.** The Trustee may also encroach on the principal of this trust in such amounts as it may deem necessary in its judgment to provide for the support of my spouse in my spouse's accustomed manner of living and to provide for the support and education of my descendants, taking into consideration any other available resources they or any of them may have to the knowledge of the Trustee.

(e) **General Intention.** My primary desire is that my spouse be supported in my spouse's accustomed manner of living during my spouse's life and that my children be supported and educated, rather than the preservation of the principal until the termination of this trust, and I wish the Trustee to be guided by this consideration in determining the amount to be used for the support of my spouse and the support and education of my descendants hereunder. After any child has completed, or in normal course should have completed, his or her education, the Trustee shall not be required to consider making any distribution for the support or education of such child or his or her descendants unless in the judgment of the Trustee there is ample property to support my spouse and support and educate my other children, or such child is unable for reasons beyond his or her control to support himself or herself.

(f) **Additional Principal Distributions.** If the purposes stated in the preceding paragraph have been satisfied or there are ample means available to satisfy them, the Trustee may at any time distribute to any child of mine a portion of the principal of this trust to enable such child to marry, to enter into a trade, profession or business, to purchase a home or for similar purposes, if the Trustee deems such distribution to be in the best interest of such child. Any distribution to such child under this paragraph shall be deducted without interest from the share of such child or his or her descendants on the division of this trust into separate shares, but the Trustee shall not be liable if the share of such child or his or her descendants remaining on such division is not sufficient to cover any such advance.

(g) **Spouse's Limited Power to Appoint.** My spouse shall have the power by instrument in writing signed by my spouse and delivered to the Trustee, or at death by last will and testament, making express reference to this power, to direct that any part or all of the property in this trust be distributed to or for the benefit of any descendant of mine, and in such manner, in trust or otherwise, as my spouse may in such instrument direct, provided that my spouse shall have no power to appoint any of said property to my spouse, to my spouse's estate, to my spouse's creditors or to the creditors of my spouse's estate.

(h) **Trusts for Descendants.** Any property remaining in this trust at the later of my death and the death of my spouse and not effectively appointed by my spouse shall be divided among my descendants then living, per stirpes, and the Trustee shall hold the resulting share of each such descendant in a separate trust for the primary benefit of such descendant as hereinafter set forth, provided that, if the inclusion ratio of this trust for generation-skipping transfer tax purposes is zero, such division shall be postponed until no then living child of mine is less than twenty-five (25) years of age (in which event the division shall be among my descendants living at the time of division, per stirpes). During any period of postponement, the trust shall be held, managed and distributed as provided by the preceding provisions of this Item.

(1) **I***ncome Distributions.* The Trustee may distribute such part, all or none of the net income of each such separate trust currently to or for the benefit of the descendant for whose primary benefit such trust is created, and his or her descendants from time to time living, in such amounts and proportions among them as the Trustee in its sole discretion shall deem best, taking into consideration any other available resources they or any of them may have to the knowledge of the Trustee. Any income not distributed currently shall be accumulated and added to the principal of the trust from which it was generated.

(2) *Principal Distributions***.** The Trustee may also encroach on the principal of each such separate trust in such amounts as it may deem necessary in its judgment to provide for the support in reasonable comfort and education of the descendant for whose primary benefit such trust is created, and his or her descendants from time to time living, taking into consideration any other available resources they or any of them may have to the knowledge of the Trustee.

(3) *Additional Principal Distributions.* The Trustee may also distribute to any descendant for whose primary benefit a trust is created hereunder, from the trust of such descendant, a portion of the principal to enable such descendant to marry, to enter into a trade, profession or business, to purchase a home or for similar purposes, if the Trustee deems such distribution to be in the best interest of such descendant.

(4) *Powers to Appoint.* Each of my descendants for whose primary benefit a trust is created hereunder shall have the power by instrument in writing signed by him or her and delivered to the Trustee, or at death by last will and testament, making express reference to this power, to direct that any part or all of his or her trust be distributed to or for the benefit of any of his or her descendants, and in such manner, in trust or otherwise, as such power holder shall so direct, provided that in no event shall this power be exercisable to appoint any of said property to the power holder, to his or her estate, to his or her creditors or to the creditors of his or her estate; except that if upon the death of the power holder, any of the trust property would otherwise be distributable to persons who are assigned, for generation-skipping transfer tax purposes, to younger generations than that of the power holder, then his or her testamentary power shall also be exercisable in favor of his or her estate.

(5) *Termination Distributions***.** If and when a descendant for whose primary benefit a trust is created hereunder has attained twenty-five (25) years of age, the Trustee shall distribute to such descendant one-third (1/3) of the property then in the trust of such

descendant; and if and when such descendant has attained thirty (30) years of age, the Trustee shall distribute to such descendant one-half (1/2) of the property then in the trust of such descendant; and if and when such descendant has attained thirty-five (35) years of age, the Trustee shall distribute to such descendant all of the property then in the trust of such descendant.

(6) *Distribution at Death.* Upon the death of a descendant for whose primary benefit a trust is created hereunder, any property remaining in such trust and not distributed by the exercise of the powers of appointment conferred above shall be divided, per stirpes, into separate trusts for his or her surviving descendants, if any, and if none, shall be divided, per stirpes, into separate trusts for the surviving descendants of mine who are descended from his or her nearest ancestor with surviving descendants of mine. Each such trust shall be deemed held for the primary benefit of the descendant of mine for whom it is created within the meaning of that phrase and similar expressions wherever used in this Item and shall be managed and distributed accordingly.

(i) **Failure of Beneficiaries.** If at any time before the final distribution of this trust all of the beneficiaries herein named or described should die and there should be no beneficiary to take the property or the income therefrom, then the property remaining in the trust shall be distributed among the persons who would have been entitled thereto under the laws of descent and distribution of the State of Georgia if I had died intestate at that time owning such property in fee simple.

ITEM V

Withdrawal Rights

Notwithstanding any other provision to the contrary herein:

(a) **Withdrawal Right of Spouse.** After each direct or indirect transfer to this trust which is treated as a gift under the federal gift tax law, my spouse shall have the absolute right and power, if then living and married to me, to withdraw from this trust an amount equal to the lesser of (i) Five Thousand Dollars ($5,000) minus the total of the amounts which were subject to the withdrawal right of my spouse in connection with previous transfers to the trust during the same calendar year, or (ii) the amount of such transfer.

(b) **Withdrawal Rights of Children.** If the amount of any such transfer to this trust exceeds the amount subject to the withdrawal right of my spouse, each then living child of mine shall have the absolute right and power to withdraw from this trust an amount equal to the lesser of (i) Five Thousand Dollars ($5,000) minus the total of the amounts which were subject to the withdrawal right of such child in connection with previous transfers to the trust during the same calendar year, or (ii) the excess of the amount of such transfer over the amount subject to the withdrawal right of my spouse, divided by the number of my then living children.

(c) **Withdrawal Rights of Children's Descendants.** If the amount of any such transfer to this trust exceeds the amount subject to the withdrawal rights of my spouse and children, each then living descendant of any child of mine shall have the absolute right and power to withdraw from this trust an amount equal to the lesser of (i) Five Thousand Dollars ($5,000) minus the total of the amounts which were subject to the withdrawal right of such descendant in connection with previous transfers to the trust during the same calendar year, or (ii) such descendant's share (determined by allocation on a per stirpes basis among the then living descendants of my then living and deceased children, making reference to me as common ancestor) of the excess of the amount of such transfer over the amount subject to the withdrawal rights of my spouse and children.

(d) **Notification.** Whenever any transfer is made that gives rise to a withdrawal right under this Item, the Trustee, upon receipt of the transferred property, shall give prompt written notice of such transfer and such withdrawal right to each person who has such right or, if any such person is under a legal disability, to the person authorized to represent him or her under the separate provision of this agreement relating to representation of persons under legal disability. Any holder of a withdrawal right, or person authorized to represent such holder, who is then acting as a Trustee of this trust shall be deemed automatically to have received the notice required to be given by the Trustee under this Item.

(e) **Exercise.** Any holder of a withdrawal right, or person authorized to represent such holder if he or she is under a legal disability, may exercise such right by delivering a written instrument to the Trustee at any time on or before the thirtieth (30th) day after receiving notice of the transfer to the trust that gives rise to the withdrawal right as provided hereinabove, or the last day of the calendar year of such transfer, whichever is earlier.

(f) **Satisfaction.** Upon receipt of a written instrument of withdrawal, the Trustee shall forthwith distribute out of the trust the amount necessary to satisfy the withdrawal right, and for this purpose the Trustee shall retain in the trust sufficient transferable assets to satisfy any outstanding and exercisable withdrawal rights. The Trustee, in satisfying any withdrawal right, may distribute cash or other property of the trust, including a share of the interest of the trust in any insurance policy, and the Trustee may borrow against the cash value of any policy to obtain cash for such distribution.

(g) **Lapse.** To the extent that a withdrawal right has not been exercised by a timely delivery of a written instrument to the Trustee as specified above, such withdrawal right shall lapse and my spouse and descendants shall forever cease to have any further withdrawal right with respect to the transfer to the trust which gave rise to the withdrawal right.

(h) **Right of Transferor to Vary.** Notwithstanding the foregoing provisions of this Item, any transferor shall have the right, by written instrument delivered to the Trustee at or before the time of the transfer but not thereafter, (i) to exclude any person who would otherwise have a withdrawal right hereunder from exercising it with respect to such transfer, (ii) to increase or decease the amount subject to such withdrawal right with respect to such transfer, or (iii) to change the period during which any withdrawal right may be exercised with respect to such transfer.

ITEM VI

Trustees

(a) **General.** During my lifetime, the individual Trustee named herein, or any successor thereto, shall act as the sole Trustee of this trust and, after my death, the corporate Trustee named herein, or any successor thereto, shall act as the sole Trustee of this trust.

(b) **Individual Trustee.** I appoint my spouse as the individual Trustee of this trust. Any individual Trustee may at any time resign as individual Trustee by instrument in writing delivered to me and to the corporate Trustee. Any resigning individual Trustee shall account to the successor Trustee of this trust as provided in Section 53-12-243(b) of the Georgia Code.

(c) **Successor Individual Trustee.** Should any vacancy occur in the office of the individual Trustee during my lifetime, then the successor individual Trustee shall be the individual whom I shall appoint by instrument in writing delivered to the predecessor individual Trustee (in case of the resignation of such predecessor), to the successor individual Trustee and to the corporate Trustee. Should I for any reason fail to appoint a successor individual Trustee within thirty (30) days, then the successor individual Trustee shall be appointed by any court having jurisdiction over this trust upon application of any person interested in the trust or upon the application of the retiring individual Trustee or such retiring Trustee's personal representative. In no event shall I be appointed successor individual Trustee of this trust.

(d) **Corporate Trustee.** I appoint SUNTRUST BANK as the corporate Trustee of this trust. Wherever SUNTRUST BANK is named herein, it shall be deemed to include any bank or trust company into which SUNTRUST BANK may hereafter be merged or consolidated.

(e) **Change of Trustee at Grantor's Death.** Upon my death, the individual Trustee shall deliver the trust property, including any property payable to such Trustee by reason of my death, to the corporate Trustee, which may assume for all purposes that the assets so delivered constitute all the assets it is entitled to hold as Trustee hereunder and which may accept such assets in the condition delivered to it by the individual Trustee.

(f) **No Audit Required; Successor's Powers.** No successor Trustee shall be required to inquire into or audit the acts or doings of any predecessor Trustee or to make any claim against any such predecessor or his or her estate. Any successor Trustee shall have and may exercise all of the powers, privileges, immunities and exemptions herein conferred on the Trustee as fully and to the same extent as if such successor had originally been named as Trustee herein.

(g) **Compensation.** An individual Trustee serving hereunder shall not receive compensation for such services, but shall be reimbursed for out-of-pocket expenses reasonably incurred in the administration of any trust created hereunder. SUNTRUST BANK shall receive as compensation for its services as Trustee the fees it normally charges to similar trusts under its regularly published fee schedule as the same may, from time to time, be amended. SUNTRUST BANK, or any of its affiliates, may also receive and retain for its own use any commission or other compensation which may be due it in connection with any insurance policy which is an asset of this trust and shall not be held thereby to have breached any duty arising in connection with this trust.

(h) **Resignation of Corporate Trustee.** The corporate Trustee may at any time resign by instrument in writing signed by such Trustee and delivered to the persons then eligible to receive income from the trusts created hereunder. Any resigning corporate Trustee shall account to the successor Trustee, if any, as provided in Section 53-12-243(b) of the Georgia Code.

(i) **Appointment of Successor Corporate Trustee.** If at any time after my death a vacancy occurs in the office of Trustee of any trust created hereunder and there is no other provision for appointing a successor, the persons who are then eligible to receive income from such trust shall, within sixty (60) days after such office becomes vacant, appoint a successor Trustee by written instrument delivered to the retiring Trustee and to the Trustee being appointed. Should such persons fail or refuse to appoint a successor within sixty (60) days, then such successor shall be appointed by any court having jurisdiction over such trust upon application of any person interested in such trust, or upon application of the retiring Trustee. Any successor Trustee appointed under this paragraph shall be a bank or trust company with trust powers and then administering trust assets (when combined with trust assets managed by other entities that control, are controlled by, or are under common control with such bank or trust company) of at least Five Hundred Million Dollars ($500,000,000).

(j) **Situs.** The original situs of administration of the trusts created hereunder shall be Georgia. The Trustee may, however, at any time and from time to time move the situs of administration of any such trust to any other state of the United States, if the Trustee determines that this step is in the best interests of the beneficiaries of the subject trust. The Trustee shall give prompt written notice of any such change of situs to the persons then eligible to receive income from such trust. If the situs of administration of any trust is moved to another state, the laws of the new situs shall govern the administration of such trust, but the construction of such trust and the rights of the beneficiaries thereof shall continue to be governed by the laws of Georgia.

(k) **Discharge of Trustee by Consent.** While I recognize that Section 53-12-231 of the Georgia Code provides a procedure for a final accounting and judicial discharge of a trustee upon resignation, removal, death or the termination of a trust, I wish to provide a more expeditious and economical settlement alternative to a judicial proceeding. Therefore, I direct that if a Trustee of any trust created hereunder ceases for any reason to serve as a Trustee, or on the termination of any such trust, the written consent of all available beneficiaries of such trust shall settle its account and relieve such Trustee from liability as against a later claim by any interested party, including those who were unborn or under a legal disability at the time of such consent, to the same extent as would a judicially approved final accounting. A beneficiary for the purposes of this paragraph shall mean any individual living at the time of such consent, or any organization in existence at such time, who or which, at any time during the period to which such settlement relates, was a distributee or permissible distributee of income or principal of such trust, or who or which, at the time of such consent, is a qualified beneficiary within the meaning of Section 53-12-2(10) of the Georgia Code. A beneficiary shall be deemed to be unavailable to give consent if the Trustee in good faith determines that such beneficiary is not competent or available within a reasonable time for this purpose; provided, however, that in connection with any such consent, an individual beneficiary who is then a minor or otherwise under legal disability shall be represented by the person authorized to represent him or her under the separate provision of this agreement relating to representation of persons under legal disability. The consent of a person who so represents another shall be binding and conclusive upon the person represented, irrespective of whether the latter is aware of the representation.

ITEM VII

Family Definitions

(a) Children and Descendants. References in this agreement to my "child," "children," "descendant" or "descendants" include those persons, if any, named as my children or other descendants earlier in this agreement, and their descendants as defined in the remaining portion of this Item. With respect to persons other than those previously named, including children born to or adopted by me after the execution of this agreement, the aforesaid terms shall refer at any given time only to persons who qualify under the rules set forth below:

(1) A person born in wedlock, or a person born out of wedlock whose parents married each other prior to the time of reference, shall be considered a descendant of both of his or her parents and of any ancestor of either of his or her parents.

(2) A person legally adopted before reaching the age of majority shall be considered a descendant of the adopting parent or parents and of any ancestor of the adopting parent or of either of the adopting parents.

(3) A person born out of wedlock shall be considered a descendant of his or her biological mother and of any ancestor of his or her biological mother.

(4) A person born out of wedlock shall be considered a descendant of his or her biological father, and of any ancestor of his or her biological father, if such father has specifically declared in a signed written instrument that such person is his child or if such person is eligible to inherit from his or her biological father under the laws of descent and distribution of the State of Georgia as in effect at the time of reference.

(b) **Spouse.** If I should cease to be married to my spouse named above prior to my death, my said spouse shall be deemed to have predeceased me for purposes of determining beneficial interests hereunder and shall be deemed to have resigned as Trustee hereunder on the date on which we cease to be married.

ITEM VIII

Accountings and Relief from Bond

The Trustee shall not be required to file any inventory or appraisal or file annual or other returns or reports to any court or to give bond. During my lifetime, the Trustee shall not be required to furnish any statements to any beneficiaries (other than notifications of withdrawal rights as provided above), and I direct that during my lifetime, (i) Section 53-12-243(a) and (b) of the Georgia Code, relating to reports and accounts to qualified beneficiaries and successor fiduciaries, and any other provisions of otherwise applicable law relating to periodic reports or accounts to beneficiaries, and (ii) Section 53-12-242(a) of the Georgia Code, requiring notification to qualified beneficiaries regarding the existence of a trust, shall not apply with respect to any trust created hereunder, except for a resigning Trustee's obligation to account to the successor Trustee under Section 53-12-243(b) of the Georgia Code. After my death, however, the Trustee shall account and furnish requested information at the times, in the manner and to the persons required by Section 53-12-243 of the Georgia Code, but Section 53-12-242(a) of the Georgia Code, requiring notification to qualified beneficiaries regarding the existence of a trust, still shall not apply with respect to any trust created hereunder. If the Trustee deems it advisable to furnish to any beneficiary, whether or not qualified, information concerning the administration of the trust beyond the required reporting, the Trustee may do so; provided that this discretionary authority shall in no way imply an obligation on the part of the Trustee to provide, or a right on the part of any such beneficiary to receive, such information.

ITEM IX

Additions to Trust

I as well as others shall have the right at any time to add to this trust by depositing additional property with the Trustee hereunder, provided such property is acceptable to the Trustee. All property so deposited shall be held, managed and distributed by the Trustee under the terms and conditions set out in this agreement, unless the instrument by which such property is deposited otherwise provides.

ITEM X

Diversification of Assets

I have confidence in the investments that have been or will be deposited hereunder, and no change need be made by the Trustee in these investments for the purpose of creating a diversity of investments. The Trustee may sell or otherwise dispose of such investments, if and to the extent the Trustee deems such sale or disposition to be in the best interest of any trust, but the Trustee shall not be required to sell or otherwise dispose of such investments and shall not be liable for failing to do so. With respect to the investments that have been or will be deposited hereunder, the Trustee shall be exempt from, and I hereby waive, any duty otherwise imposed by Section 53-12-341 of the Georgia Code or by any other statute or principle of law to manage the risk of concentrated holdings by diversifying or by using other mechanisms.

ITEM XI

Rule Against Perpetuities

(a) **Vesting.** Anything in this agreement to the contrary notwithstanding, all property of every trust created herein and not otherwise vested under any provision hereof shall vest in and be distributed to the persons then entitled to the income from such property at the expiration of twenty-one (21) years after the death of the last surviving beneficiary hereunder who was in life at the date of the execution of this agreement. The purpose of this provision is to prevent any possible violation of the rule against perpetuities, and this provision should be so construed.

(b) **Discretionary Distribution.** If the persons to receive the income from any property, or the amount of such income to be received by each person, are to be determined in the discretion of the Trustee, then the Trustee shall distribute such property among such of the persons to whom the Trustee is authorized to distribute income, and in such proportions, as the Trustee in its discretion shall determine.

ITEM XII

Powers and Administration

(a) **Powers.** In the management, care and disposition of this trust, the Trustee, and the Trustee's successors in office, shall have the power to do all things and to execute such instruments as may be deemed necessary or proper, including the following powers, all of which may be exercised without order of or report to any court:

(1) **Sale.** To sell, exchange or otherwise dispose of any property at any time held or acquired hereunder, at public or private sale, for cash or on terms, without advertisement, including the right to lease for any term notwithstanding the period of the trust, and to grant options (including writing covered call options) to buy for any period, including a period beyond the duration of the trust;

(2) **Investment.** To invest all monies in such stocks, bonds, securities, investment company or trust shares, mortgages, notes, choses in action, real estate, improvements thereon, interests in partnerships, limited liability companies and other entities (including interests in investment companies or trusts and in collective or commingled investment funds offered or advised by or through the corporate Trustee or any of its affiliates, and interests in any entity to which the corporate Trustee or any of its affiliates renders investment advice or other services for compensation), and other property of any kind, real or personal, as the Trustee may deem best without regard to any law or regulation now or hereafter in force limiting investments of fiduciaries or the fact that a security is purchased from an underwriting syndicate that includes the Trustee or an affiliate of the Trustee as a member or that the security was underwritten by such a syndicate and is purchased from a member of that syndicate;

(3) **Retention.** To retain for investment any property or choses in action deposited with the Trustee hereunder, including any stock in any corporate Trustee or in a parent or affiliate company of such Trustee or in a company whose stock any corporate Trustee or its parent or affiliate holds as an asset, either individually or in a fiduciary capacity; but this power of retention is subject to any provisions of this agreement directing the Trustee to manage the risk of concentrated holdings of assets by diversification or other appropriate mechanisms;

(4) **Voting.** To vote in person or by proxy any corporate stock or other security or ownership interest and to agree to or take any other action in regard to any reorganization, merger, consolidation, liquidation, bankruptcy or other procedure or proceeding affecting any stock, bond, note or other security or ownership interest;

(5) **Agents.** To employ attorneys, real estate brokers, accountants, investment managers, investment advisors and other agents, including affiliates of the corporate Trustee, if such employment be deemed appropriate, to rely reasonably on the advice of such agents, and to pay reasonable compensation for their services;

(6) **Claims.** To compromise, settle or adjust any claim or demand by or against the trust and to agree to any rescission or modification of any contract or agreement affecting the trust;

(7) **Borrowing.** To renew any indebtedness, as well as to borrow money, and to secure the same by mortgaging, pledging or conveying any property of the trust, including the power to borrow from the Trustee or any of the corporate Trustee's affiliates at a reasonable rate of interest;

(8) **Business Interests.** To retain and carry on any business in which the trust acquires an interest, to acquire additional interests in any such business, to agree to the liquidation in kind of any corporation or other entity in which the trust may have an interest and to carry on the business thereof, to join with other owners in adopting any form of management for any business or property in which the trust may have an interest, to become or remain a partner, general or limited, in regard to any such business or property, to incorporate any such business or property or to form a limited liability company or other entity with respect thereto (including any such entity to which the corporate Trustee or any of its affiliates renders investment advice or other services) and to hold the stock or other ownership interest as an investment, and to employ agents and confer on them authority to manage and operate such business, property, corporation or other entity, without liability for the acts of any such agents or for any loss, liability or indebtedness of such business if the management is selected or retained with reasonable care;

(9) **Registration with Nominee.** To register any stock, bond, or other security in the name of a nominee, and use nationally and internationally recognized depositories, without the addition of words indicating that such security is held in a fiduciary capacity; but accurate records shall be maintained showing that such security is a trust asset; and

(10) **Environmental Issues.** To pay from any trust created hereunder all charges which the Trustee deems necessary or appropriate to comply with laws regulating environmental conditions and to remedy or ameliorate any such conditions which the Trustee determines adversely affect such trust or otherwise are liabilities of such trust, and to pay any liabilities, fines or penalties incurred by the Trustee, either in its fiduciary capacity or personally, on account of such conditions and arising out of the performance of its duties hereunder, other than any such charges which are directly caused by its own gross negligence or willful misconduct, and to apportion all of such charges among the several trusts hereunder and the interests of the beneficiaries therein in such manner as the Trustee reasonably deems fair, prudent and equitable under all of the circumstances.

(b) **Beneficiaries under Age 25.** Whenever the Trustee is directed to distribute any trust property in fee simple to a person who is then under twenty-five (25) years of age, the Trustee may hold such property in trust for such person until he or she becomes twenty-five (25) years of age, and in the meantime shall use such part of the income and the principal of the trust as the Trustee may deem necessary to provide for the support in reasonable comfort and education of such person. Any income not distributed currently shall be accumulated and added to the principal of the trust. If the person for whom such trust is held should die before becoming twenty-five (25) years of age, the property then remaining in the trust shall be distributed to the personal representative of such person's estate.

(c) **Minor or Disabled Beneficiaries.** In making distributions from any trust created hereunder to or for the benefit of any minor or other person under a legal disability, the Trustee need not require the appointment of a conservator, but may distribute the same to the custodian of such person or to the custodian under any applicable transfers to minors act (or, in the case of a beneficiary other than my spouse, to any existing trust for his or her exclusive benefit), may distribute the same to such person without the intervention of a conservator, may distribute the same to a conservator of such person's estate if one has already been appointed, or may use the same for the benefit of such person.

(d) **Representation.** Except as provided in the immediately preceding paragraph, for all purposes under this agreement, including but not limited to delivery of statements by the Trustee, delivery of notice of a Trustee's resignation, and any exercise of consent or other discretionary rights conferred upon beneficiaries, including any withdrawal right, a beneficiary who is then a minor or otherwise under legal disability shall be represented by the then acting conservator of his or her estate, if any, otherwise by his or her natural or legal guardian; provided, however, that any inter vivos power of appointment of such beneficiary, other than a withdrawal right, shall be exercisable only by the then acting conservator of his or her estate, if any, and only to the extent permitted by then applicable Georgia law. This paragraph shall not, however, confer on me any power in any capacity, alone or in conjunction with any person, to affect the beneficial enjoyment of any trust property through the exercise of a power to alter, amend, revoke, terminate or otherwise.

(e) **Division and Distribution in Kind.** In the distribution of the trust and the division into separate trusts and shares, the Trustee may make the distribution and division in money or in kind or in both, regardless of the basis for income tax purposes of any property distributed or divided in kind, and the distribution and division made and the values established by the Trustee shall be binding and conclusive on all persons taking hereunder. The Trustee may, in making such distribution or division, allot undivided interests in the same property to several trusts or shares.

(f) **Allocation of Income and Expenses.** The Trustee shall have discretion to determine whether items should be charged or credited to income or principal or allocated between income and principal as the Trustee may deem equitable and fair under all the circumstances, including the power to amortize or fail to amortize any part or all of any premium or discount, to treat any part or all of the profit resulting from the maturity or sale of any asset, whether purchased at a premium or at a discount, as income or principal or apportion the same between income and principal, to apportion the sales price of any asset between income and principal, to treat any dividend or other distribution on any investment as income or principal or apportion the same between income and principal, to charge any expense against income or principal or apportion the same, and to provide or fail to provide a reasonable reserve against depreciation or obsolescence, all as the Trustee may reasonably deem equitable and just under all the circumstances.

(g) **Transactions Between Related Parties.** The Trustee may lend to or borrow from, at an adequate rate of interest and with adequate security and upon such terms and conditions as the Trustee shall deem fair and equitable, and may sell any property to, or purchase any property from, at the fair market value thereof as determined by the Trustee, my estate, or the estate of my spouse or the estate of any descendant of mine or any trust created by me, by my spouse or by any descendant of mine, by will or during life, even though the same person or corporation may be acting as trustee of any of such other trusts or as personal representative of my estate or of the estate of my spouse or such descendant of mine.

(h) **Small Trust Termination.** If at any time the total fair market value of the assets of any trust, other than any qualified charitable split-interest trust, created or to be created hereunder is so small that the corporate Trustee's annual fee for administering the trust would be the minimum annual fee set out in the Trustee's regularly published fee schedule then in effect, the Trustee in its discretion may terminate such trust or may decide not to create such trust, and in such event the property then held in or to be distributed to such trust shall be distributed to the persons who are then or would be entitled to the income of such trust. If the persons to receive the income from any property, or the amount of such income to be received by each person, are to be determined in the discretion of the Trustee, then the Trustee shall distribute such property among such of the persons to whom the Trustee is authorized to distribute income, and in such proportions, as the Trustee in its discretion shall determine.

(i) **Division and Consolidation of Trusts.** The Trustee may for tax, administrative or investment purposes divide any transfer in trust provided for hereunder, based upon the fair market values of the transferred property at the time of division, into two or more fractional shares to be held as separate trusts, the dispositive provisions of which, except as otherwise expressly provided herein, shall be identical to those that would have been applicable to the trust had the division not occurred, and consolidate any trust created hereunder with any trust having substantially identical provisions for the same beneficiary or beneficiaries if such consolidation is consistent with my intent and does not defeat or impair a beneficial interest. Without limiting the generality of the foregoing, the Trustee may divide any trust into separate trusts consisting of portions that would, and would not, respectively, be included in the gross estate of my spouse or another beneficiary for federal estate tax purposes if such beneficiary died immediately prior to the division. The Trustee may also divide any transfer in trust provided for hereunder into fractional shares to which all, and none, respectively, of my or my spouse's remaining GST exemption may be allocated, so as to create two separate trusts, the dispositive provisions of which, except as otherwise expressly provided herein, shall be identical to those which would have applied if such transfer had not been divided.

(j) **References.** Except as otherwise expressly provided herein, references herein to the "Internal Revenue Code" mean the Internal Revenue Code of 1986 and any successor statute, references to the "Georgia Code" mean the Official Code of Georgia Annotated and any successor statute, and references to a provision of either such Code include such provision as it may be amended and the corresponding provision of any successor statute.

(k) **Titles.** The descriptive word headings used in this agreement are for convenience of reference only, shall be disregarded in interpreting and construing this agreement, and shall not be deemed to affect the meaning of any provision hereof.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my seal and, to evidence acceptance of the trust herein created, the individual Trustee has hereunto set the individual Trustee's hand and affixed the individual Trustee's seal, this ____ day of __________, ____.

__________________________(SEAL)

Grantor

__________________________(SEAL)

Individual Trustee

Signed, sealed and delivered this

____ day of ______________, ____

in the presence of:

____

Unofficial Witness

____

Notary Public [SEAL]

Approved:

____

Attorney for Grantor

GRANTOR RETAINED ANNUITY TRUST FORM

I hereby transfer, assign and convey to SUNTRUST BANK (hereinafter called the "Trustee"), as Trustee, the property shown on the attached schedule, in trust for the beneficiaries to be held, managed and distributed upon the uses and trusts hereinafter set out.

ITEM I

Irrevocable

I have been fully advised and understand and declare that this trust is and shall be irrevocable, and, except as expressly provided herein, I shall have no right, title or interest in or power, privilege or incident of ownership in regard to any of the property in this trust and no right to alter, amend, modify, revoke or terminate this trust or any of its provisions. My interest and the interest of my estate in this trust shall not be subject to commutation.

ITEM II

Family

On the date of execution of this agreement, I am married to _____________, sometimes referred to in this agreement as "my spouse," and my living children are ___________________, ____________________ and _______________.

ITEM III

Purpose of Trust

My interest (and that of my estate) in the trust during the annuity term, as hereinafter defined (the "annuity interest"), is intended to qualify as a qualified interest, as described in Section 2702(b) of the Internal Revenue Code, and as a qualified annuity interest, as described in Sections 25.2702-3(b) and (d) of the Treasury Regulations, or any modification or replacement thereof, and this trust shall be administered and construed accordingly. The Trustee shall not have any power or responsibility under the provisions of this agreement or under applicable laws which would cause the annuity interest to fail to qualify as a qualified interest or qualified annuity interest. Should any provision of this agreement be inconsistent or in conflict with any applicable requirement for a qualified annuity interest, then such requirement shall be deemed to override and supersede that inconsistent or conflicting provision. Any required provision of a qualified annuity interest that is omitted from this agreement shall be incorporated herein by reference and shall apply retroactively, if necessary, and be deemed to be a part of this agreement to the same extent as though expressly set forth herein. I specifically empower the Trustee, acting alone, to amend this agreement during the annuity term for the sole purpose of ensuring that the trust complies with and continues to comply with the applicable requirements for a qualified annuity interest and, if necessary, any such amendment shall apply retroactively to the inception of this trust. All other provisions of this agreement shall be subordinate to this Item.

ITEM IV

Distributions

(a) **Annuity.** During the period commencing on the date of execution of this agreement and terminating on the ________ anniversary of such date (the "annuity term"), the Trustee shall distribute to me on each anniversary of the date of execution of this agreement during the annuity term an amount equal to ________ percent (__%) of the initial net fair market value of the assets passing into the trust, as finally determined for federal transfer tax purposes (the "annuity amount"). The annuity amount shall be paid annually from income and, to the extent that income is not sufficient, from principal. Any income of the trust in excess of the annuity amount shall be added to principal.

(b) **Death of Grantor During Annuity Term.** If I die before the end of the annuity term, all remaining distributions of the annuity amount shall be made to the personal representative of my estate in the manner provided in paragraph (a) of this Item.

(c) **Incorrect Valuations.** If the initial net fair market value of the trust assets is incorrectly determined, then, within a reasonable period after the value is finally determined for federal transfer tax purposes, the Trustee shall distribute to me or to my estate (in the case of an undervaluation) or receive from me or from my estate (in the case of an overvaluation) an amount equal to the difference between the annuity amount properly distributable and the annuity amount actually distributed.

(d) **Short Years.** In determining the annuity amount, the Trustee shall prorate the same on a daily basis to the extent required by the Treasury Regulations applicable to qualified annuity interests.

(e) **Termination.** Upon the expiration of the annuity term, all property then remaining in the trust shall, subject to the satisfaction of the Trustee's obligations under the other provisions of this Item, be divided into as many separate and equal shares as I have children then living and deceased children with descendants then living, and the Trustee shall distribute one such share to each then living child of mine, one such share to the personal representative of the estate of each child of mine who died during the annuity term and has descendants living at the expiration of the annuity term, and one such share per stirpes among the descendants, living at the expiration of the annuity term, of each child of mine who predeceased the date of execution of this agreement.

(f) **Taxable Year.** The first taxable year of the trust shall begin with the date of this agreement and shall end on the following December 31. Subsequent taxable years shall be calendar years.

(g) **Prohibited Distributions.** Notwithstanding anything in this agreement to the contrary, (i) during the annuity term, no distributions shall be made from the trust to or for the benefit of any person, other than the distributions to me or my estate as set forth above, and (ii) the Trustee is prohibited from issuing a note, other debt instrument, option or other similar financial arrangement in satisfaction of the annuity distribution obligation.

ITEM V

No Additions

No additional contributions shall be made to the trust by me or by any other person after the initial contribution.

ITEM VI

Family Definitions

References in this agreement to my "child," "children," "descendant" or "descendants" include those persons, if any, named as my children or other descendants earlier in this agreement, and their descendants as defined in the remaining portion of this Item. With respect to persons other than those previously named, including children born to or adopted by me after the execution of this agreement, the aforesaid terms shall refer at any given time only to persons who qualify under the rules set forth below:

(a) A person born in wedlock, or a person born out of wedlock whose parents married each other prior to the time of reference, shall be considered a descendant of both of his or her parents and of any ancestor of either of his or her parents.

(b) A person legally adopted before reaching the age of majority shall be considered a descendant of the adopting parent or parents and of any ancestor of the adopting parent or of either of the adopting parents.

(c) A person born out of wedlock shall be considered a descendant of his or her biological mother and of any ancestor of his or her biological mother.

(d) A person born out of wedlock shall be considered a descendant of his or her biological father, and of any ancestor of his or her biological father, if such father has specifically declared in a signed written instrument that such person is his child or if such person is eligible to inherit from his or her biological father under the laws of descent and distribution of the State of Georgia as in effect at the time of reference.

ITEM VII

Accountings and Relief from Bond

The Trustee shall not be required to file any inventory or appraisal or file annual or other returns or reports to any court or to give bond, but shall (i) account and furnish requested information at the times, in the manner and to the persons required by Section 53-12-243 of the Georgia Code, and (ii) comply with Section 53-12-242(a) of the Georgia Code, requiring notification to qualified beneficiaries regarding the existence of a trust. If the Trustee deems it advisable to furnish to any beneficiary, whether or not qualified, information concerning the administration of the trust beyond the required reporting, the Trustee may do so; provided that this discretionary authority shall in no way imply an obligation on the part of the Trustee to provide, or a right on the part of any such beneficiary to receive, such information.

ITEM VIII

Power to Substitute Assets

I expressly reserve the right, exercisable in a nonfiduciary capacity without the approval or consent of any person in a fiduciary capacity, during my lifetime, to reacquire some or all of the property of this trust by substituting property of equivalent value. By virtue of the provisions of this Item, it is intended that during my lifetime or until I renounce such power, I shall be treated, pursuant to Section 675(4)(C) of the Internal Revenue Code, as the owner of the income and principal of this trust for federal income tax purposes.

ITEM IX

Diversification of Assets

I have confidence in the investments that have been deposited hereunder, and no change need be made by the Trustee in these investments for the purpose of creating a diversity of investments. The Trustee may sell or otherwise dispose of such investments, if and to the extent the Trustee deems such sale or disposition to be in the best interest of this trust, but the Trustee shall not be required to sell or otherwise dispose of such investments and shall not be liable for failing to do so. With respect to the investments that have been deposited hereunder, the Trustee shall be exempt from, and I hereby waive, any duty otherwise imposed by Section 53-12-341 of the Georgia Code or by any other statute or principle of law to manage the risk of concentrated holdings by diversifying or by using other mechanisms. Nothing in this agreement shall be construed to restrict the Trustee from investing the trust assets in a manner that could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets.

ITEM X

Trustees

(a) **Merger of Corporate Trustee.** Wherever SUNTRUST BANK is named herein, it shall be deemed to include any bank or trust company into which SUNTRUST BANK may hereafter be merged or consolidated.

(b) **Compensation.** SUNTRUST BANK shall receive as compensation for its services as Trustee the fees it normally charges to similar trusts under its regularly published fee schedule as the same may, from time to time, be amended.

(c) **Resignation.** Any Trustee hereunder may at any time resign by instrument in writing signed by such Trustee and delivered to me, if then living, and to the persons then eligible to receive income from the trusts created hereunder. Any resigning Trustee shall account to the successor Trustee, if any, as provided in Section 53-12-243(b) of the Georgia Code.

(d) **Appointment of Successor Trustee.** If a vacancy occurs in the office of Trustee of any trust created hereunder and there is no other provision for appointing a successor, the persons who are then eligible to receive income from such trust shall, within sixty (60) days after such office becomes vacant, appoint a successor Trustee by written instrument delivered to the retiring Trustee and to the Trustee being appointed. Should such persons fail or refuse to appoint a successor within sixty (60) days, then such successor shall be appointed by any court having jurisdiction over such trust upon application of any person interested in such trust, or upon application of the retiring Trustee. Any successor Trustee appointed hereunder shall be a bank or trust company with trust powers and then administering trust assets (when combined with trust assets managed by other entities that control, are controlled by, or are under common control with such bank or trust company) of at least Five Hundred Million Dollars ($500,000,000).

(e) **No Audit Required; Successor's Powers.** No successor Trustee shall be required to inquire into or audit the acts or doings of any predecessor Trustee or to make any claim against any such predecessor or his or her estate. Any successor Trustee shall have and may exercise all of the powers, privileges, immunities and exemptions herein conferred on the Trustee as fully and to the same extent as if such successor had originally been named as Trustee herein.

(f) **Situs.** The original situs of administration of the trusts created hereunder shall be Georgia. The Trustee may, however, at any time and from time to time move the situs of administration of any such trust to any other State of the United States, if the Trustee determines that this step is in the best interests of the beneficiaries of the subject trust. The Trustee shall give prompt written notice of any such change of situs to the persons then eligible to receive income from such trust. If the situs of administration of any trust is moved to another State, the administration of such trust shall be governed by the laws of the new situs, but the construction of such trust and the rights of the beneficiaries thereof shall continue to be governed by the laws of Georgia.

(g) **Discharge of Trustee by Consent.** While I recognize that Section 53-12-231 of the Georgia Code provides a procedure for a final accounting and judicial discharge of a trustee upon resignation, removal, death or the termination of a trust, I wish to provide a more expeditious and economical settlement alternative to a judicial proceeding. Therefore, I direct that if a Trustee of any trust created hereunder ceases for any reason to serve as a Trustee, or on the termination of any such trust, the written consent of all available beneficiaries of such trust shall settle its account and relieve such Trustee from liability as against a later claim by any interested party, including those who were unborn or under a legal disability at the time of such consent, to the same extent as would a judicially approved final accounting. A beneficiary for the purposes of this paragraph shall mean any individual living at the time of such consent, or any organization in existence at such time, who or which, at any time during the period to which such settlement relates, was a distributee or permissible distributee of income or principal of such trust, or who or which, at the time of such consent, is a qualified beneficiary within the meaning of Section 53-12-2(10) of the Georgia Code. A beneficiary shall be deemed to be unavailable to give consent if the Trustee in good faith determines that such beneficiary is not competent or available within a reasonable time for this purpose; provided, however, that in connection with any such consent, an individual beneficiary who is then a minor or otherwise under legal disability shall be represented by the person authorized to represent him or her under the separate provision of this agreement relating to representation of persons under legal disability. The consent of a person who so represents another shall be binding and conclusive upon the person represented, irrespective of whether the latter is aware of the representation.

ITEM XI

Powers and Administration

(a) **Powers.** In the management, care and disposition of this trust, the Trustee, and its successors in office, shall have the power, subject to the foregoing provisions of this agreement and to the extent consistent with the qualification of the annuity interest as a qualified annuity interest, to do all things and to execute such instruments as may be deemed necessary or proper, including the following powers, all of which may be exercised without order of or report to any court:

(1) **Sale.** To sell, exchange or otherwise dispose of any property at any time held or acquired hereunder, at public or private sale, for cash or on terms, without advertisement, including the right to lease for any term notwithstanding the period of the trust, and to grant options (including writing covered call options) to buy for any period, including a period beyond the duration of the trust;

(2) **Investment.** To invest all monies in such stocks, bonds, securities, investment company or trust shares, mortgages, notes, choses in action, real estate, improvements thereon, interests in partnerships, limited liability companies and other entities (including interests in investment companies or trusts and in collective or commingled investment funds offered or advised by or through the corporate Trustee or any of its affiliates, and interests in any entity to which the corporate Trustee or any of its affiliates renders investment advice or other services for compensation), and other property of any kind, real or personal, as the Trustee may deem best without regard to any law or regulation now or hereafter in force limiting investments of fiduciaries or the fact that a security is purchased from an underwriting syndicate that includes the Trustee or an affiliate of the Trustee as a member or that the security was underwritten by such a syndicate and is purchased from a member of that syndicate;

(3) **Retention.** To retain for investment any property or choses in action deposited with the Trustee hereunder, including any stock in any corporate Trustee or in a parent or affiliate company of such Trustee or in a company whose stock any corporate Trustee or its parent or affiliate holds as an asset, either individually or in a fiduciary capacity; but this power of retention is subject to any provisions of this agreement directing the Trustee to manage the risk of concentrated holdings of assets by diversification or other appropriate mechanisms;

(4) **Voting.** To vote in person or by proxy any corporate stock or other security or ownership interest and to agree to or take any other action in regard to any reorganization, merger, consolidation, liquidation, bankruptcy or other procedure or proceeding affecting any stock, bond, note or other security or ownership interest;

(5) **Agents.** To employ attorneys, real estate brokers, accountants, investment managers, investment advisors and other agents, including affiliates of the corporate Trustee, if such employment be deemed appropriate, to rely reasonably on the advice of such agents, and to pay reasonable compensation for their services;

(6) **Claims.** To compromise, settle or adjust any claim or demand by or against the trust and to agree to any rescission or modification of any contract or agreement affecting the trust;

(7) **Borrowing.** To renew any indebtedness, as well as to borrow money, and to secure the same by mortgaging, pledging or conveying any property of the trust, including the power to borrow from the Trustee or any of the corporate Trustee's affiliates at a reasonable rate of interest;

(8) **Business Interests.** To retain and carry on any business in which the trust acquires an interest, to acquire additional interests in any such business, to agree to the liquidation in kind of any corporation or other entity in which the trust may have an interest and to

carry on the business thereof, to join with other owners in adopting any form of management for any business or property in which the trust may have an interest, to become or remain a partner, general or limited, in regard to any such business or property, to incorporate any such business or property or to form a limited liability company or other entity with respect thereto (including any such entity to which the corporate Trustee or any of its affiliates renders investment advice or other services) and to hold the stock or other ownership interest as an investment, and to employ agents and confer on them authority to manage and operate such business, property, corporation or other entity, without liability for the acts of any such agents or for any loss, liability or indebtedness of such business if the management is selected or retained with reasonable care;

(9) **Registration with Nominee.** To register any stock, bond or other security in the name of a nominee, and use nationally and internationally recognized depositories, without the addition of words indicating that such security is held in a fiduciary capacity; but accurate records shall be maintained showing that such security is a trust asset; and

(10) **Environmental Issues.** To pay from any trust created hereunder all charges which the Trustee deems necessary or appropriate to comply with laws regulating environmental conditions and to remedy or ameliorate any such conditions which the Trustee determines adversely affect such trust or otherwise are liabilities of such trust, and to pay any liabilities, fines or penalties incurred by the Trustee, either in its fiduciary capacity or personally, on account of such conditions and arising out of the performance of its duties hereunder, other than any such charges which are directly caused by its own gross negligence or willful misconduct, and to apportion all such charges among the several trusts hereunder and the interests of the beneficiaries therein in such manner as the Trustee reasonably deems fair, prudent and equitable under all of the circumstances.

(b) **Beneficiaries Under Age 25.** After the annuity term, whenever the Trustee is directed to distribute any trust property in fee simple to a person who is under twenty-five (25) years of age at the time for such distribution, the Trustee may hold such property in trust for such person until he or she becomes twenty-five (25) years of age, and in the meantime shall use such part of the income and the principal of the trust as the Trustee may deem necessary to provide for the support in reasonable comfort and education of such person. Any income not distributed currently shall be accumulated and added to the principal of the trust. If the person for whom such trust is held should die before becoming twenty-five (25) years of age, the property then remaining in the trust shall be distributed to the personal representative of such person's estate.

(c) **Minor or Disabled Beneficiaries.** In making distributions from any trust created hereunder to or for the benefit of any minor or other person under a legal disability, the Trustee need not require the appointment of a conservator, but may distribute the same to the custodian of such person or to the custodian under any applicable transfers to minors act (or, in the case of a beneficiary other than my spouse or me, to any existing trust for his or her exclusive benefit), may distribute the same to such person without the intervention of a conservator, may distribute the same to a conservator of such person's estate if one has already been appointed, or may use the same for the benefit of such person.

(d) **Representation.** Except as provided in the immediately preceding paragraph, for all purposes under this agreement, including but not limited to delivery of statements by the Trustee, delivery of notice of a Trustee's resignation, and any exercise of consent or other discretionary rights conferred upon beneficiaries, a beneficiary who is then a minor or otherwise under legal disability shall be represented by the then acting conservator of his or her estate, if any, otherwise by his or her natural or legal guardian. This paragraph shall not, however, confer on me any power in any capacity, alone or in conjunction with any person, to affect the beneficial enjoyment of any trust property through the exercise of a power to alter, amend, revoke, terminate or otherwise.

(e) **Division and Distribution in Kind.** In the distribution of the trust and the division into separate trusts and shares, the Trustee may make the distribution and division in money or in kind or both, regardless of the basis for income tax purposes of any property distributed or divided in kind, and the distribution and division made and the values established by the Trustee shall be binding and conclusive on all persons taking hereunder. The Trustee may, in making such distribution or division, allot undivided interests in the same property to several trusts or shares.

(f) **Allocation of Income and Expenses.** The Trustee shall have discretion to determine whether items should be charged or credited to income or principal or allocated between income and principal as the Trustee may deem equitable and fair under all the circumstances, including the power to amortize or fail to amortize any part or all of any premium or discount, to treat any part or all of the profit resulting from the maturity or sale of any asset, whether purchased at a premium or at a discount, as income or principal or apportion the same between income and principal, to apportion the sales price of any asset between income and principal, to treat any dividend or other distribution on any investment as income or principal or apportion the same between income and principal, to charge any expense against income or principal or apportion the same, and to provide or fail to provide a reasonable reserve against depreciation or obsolescence, all as the Trustee may reasonably deem equitable and just under all the circumstances.

(g) **Transactions Between Related Parties.** The Trustee may lend to or borrow from, at an adequate rate of interest and with adequate security and upon such terms and conditions as the Trustee shall deem fair and equitable, and may sell any property to, or purchase any property from, at the fair market value thereof as determined by the Trustee, my estate, or the estate of my spouse or the estate of any descendant of mine or any trust created by me, by my spouse or by any descendant of mine, by will or during life, even though the same person or corporation may be acting as trustee of any of such other trusts or as personal representative of my estate or of the estate of my spouse or such descendant of mine.

(h) **Division and Consolidation of Trusts.** After the annuity term, the Trustee may for tax, administrative or investment purposes divide any transfer in trust provided for hereunder, based upon the fair market values of the transferred property at the time of division, into two or more fractional shares to be held as separate trusts, the dispositive provisions of which, except as otherwise expressly provided herein, shall be identical to those that would have been applicable to the trust had the division not occurred, and consolidate any trust created hereunder with any trust having substantially identical provisions for the same beneficiary or beneficiaries if such consolidation is consistent with my intent and does not defeat or impair a beneficial interest.

(i) **References.** Except as otherwise expressly provided herein, references herein to the "Internal Revenue Code" mean the Internal Revenue Code of 1986 and any successor statute, references to the "Georgia Code" mean the Official Code of Georgia Annotated and any successor statute, and references to a provision of either such Code include such provision as it may be amended and the corresponding provision of any successor statute.

(j) **Titles.** The descriptive word headings used in this agreement are for convenience of reference only, shall be disregarded in interpreting and construing this agreement, and shall not be deemed to affect the meaning of any provision hereof.

IN WITNESS WHEREOF I have hereunto set my hand and affixed my seal and, to evidence acceptance of the trust herein created, the Trustee has caused this instrument to be signed by its duly authorized officer, this _______ day of ____________, ____.

_________________________(SEAL)

Grantor

SUNTRUST BANK, Trustee

By:______________________(SEAL)

Title:

Signed, sealed and delivered this ____ day

of ______________, ____ in the presence of:

Unofficial Witness

Notary Public [SEAL]

Approved:

Attorney for Grantor

SCHEDULE

Estate Planning for the Disabled

Submitted by Dennise L. Grayson

V. ESTATE PLANNING FOR THE DISABLED

Written by Dennise L. Grayson

I. Estate Planning Considerations for Families Affected by a Disability

When estate planning, it is important to consider whether the client or a member of their family is disabled. Many disabled individuals rely on means-tested governmental benefits such as Supplemental Security Income ("SSI") and Medicaid. Means tested benefits are only available to people who qualify based on financial hardship.

For clients or heirs who are disabled, strategic estate planning can be extremely important to ensure the person will qualify for the benefits they may need in the future and also protect certain assets.

It is important to consider the effect a client's estate plan may have on their family member's eligibility for public benefits. A well-meaning grandparent who leaves a significant amount of their estate to a disabled grandchild may actually harm the grandchild by disqualifying their eligibility for Medicaid, and thus eliminate the accessibility of services that are restricted to Medicaid eligible individuals.

In many cases, the solution for families with these special circumstances is a Supplemental Needs Trust, more commonly known as a "Special Needs Trust." These trusts are not only used to maintain eligibility for public benefits, but also to supplement what is covered by public benefits so that the disabled individual can enjoy a better quality of life.

II. The Types of Special Needs Trusts and Their Specific Purposes

A Special Needs Trust ("SNT") is a discretionary spendthrift trust created for a beneficiary with a disability, which provides that the assets will be used to supplement but not replace, public benefits for which the beneficiary is eligible.[1] It is generally used to limit a trustee's discretion as to the purpose of the distributions so as not to interrupt the beneficiary's eligibility for any public benefits. In other words, the assets in the Special Needs Trust do not count against the beneficiary for Medicaid eligibility.[2]

The Georgia Department of Community Health requires that all Special Needs Trusts be submitted to DCH for approval before they are signed and an annual accounting is due for each trust after approval. [3]

In addition to an income-only or "Miller" trust, there are three main types of Special Needs Trusts: self-settled d4A; self-settled d4C; and third party trusts. The terms self-settled and third party refer to the how the trust is funded (whether it is the beneficiary's own funds used to create the trust or the funds of another person).

Self-settled trusts are commonly referred to as "Medicaid payback trusts" because at the death of the beneficiary, the trust assets are used to reimburse Medicaid as part of the estate recovery.

A. Self-settled d4A trusts

Governed by 42 USC §1396p(d)(4)(A), this type of self settled special needs trust is commonly referred to as a "d4A Trust." These are established using the beneficiary's own funds.

To qualify for and establish a d4A trust, the individual must be under the age of 65 and disabled, as defined in §1614(a)(3). Since new law was enacted in 2017, a mentally competent individual can now establish the trust themselves. Alternatively, the trust may be established by a Guardian, Parent, Grandparent, or by Court Order.

[1] POMS SI 01120.200.B.13.
[2] 42 U.S.C. §1396p(c)(2)(B)(iv).
[3] Send to: Department of Community Health Trust Unit, 900 Circle 75 Parkway SE, Suite 650, Atlanta, GA 30339

This type of trust is often used as a "fix" for when a person receiving means-tested benefits such as SSI receives an inheritance that would otherwise make that person ineligible for continued Medicaid. This type of trust can also be used for personal injury settlements; but in that instance, a Medicare Set Aside trust might also be necessary.

Self-settled special needs trusts must be irrevocable. If the trust is not irrevocable, then the trust principal is considered to be available to the beneficiary and thus considered a resource for benefit eligibility purposes.[4] These trusts must also be established for the **sole benefit** of the disabled beneficiary.[5]

Also, a d4A trust **must include a Medicaid payback** at the beneficiary's death to cover all medical expenses paid by Medicaid during the beneficiary's life.[6]

B. Self-Settled d4C Trusts

Self-settled d4C trusts are similar to the d4A trust above but are established as a pooled trust. This trust is governed by 42 USC §1396p(d)(4)(C). These trusts are managed by a non-profit organization.[7] The non-profit organization that manages the funds maintains a separate account for each beneficiary, but assets of all trusts under their management are pooled together to produce a better return on investments.[8]

When creating a d4C trust, one must first determine who can establish the trust. If the beneficiary does not have capacity, their Guardian, Parent, Grandparent or Conservator must establish the trust. If the beneficiary does have capacity, they can join the pooled trust and transfer their assets to the trust, without needing involvement of a court, parent, grandparent or

[4] GEORGIA MEDICAID MANUAL §2346-3 ("if the trust is irrevocable and cannot be used by the [applicant/recipient] for his/her support and maintenance, it is not a resource. If the [applicant/recipient] does not have the legal authority to revoke the trust or direct the use of the trust assets, the trust principal is not the [applicant/recipient]'s resource").
[5] 42 U.S.C. §1396p(d)(4)(A); GEORGIA MEDICAID MANUAL §2346.
[6] *See* GEORGIA MEDICAID MANUAL §2346.
[7] 42 U.S.C. §1396p(d)(4)(C)(i).
[8] *See* 42 U.S.C. §1396p(d)(4)(C)(ii).

guardian. Another benefit of a pooled trust over a d4A trust, is that pooled trusts do not have to be established before the individual turns 65, although in some states, a transfer penalty may apply if the individual is over 65 years of age.

To qualify as a d4C trust, the trust must provide that on the death of the beneficiary, the State is reimbursed for any Medicaid assistance it paid on behalf of the beneficiary, and any remaining principal is retained by the Trust for other disabled individuals.[9] Generally, this Medicaid repayment must be satisfied upon the death of the beneficiary prior to other expenses, such as the beneficiary's funeral expenses.

There are several approved pooled trusts in Georgia. Contact Department of Community Health for a current listing of approved trusts. Some pooled trusts do not accept real property, so be sure to inquire specifically the type of assets the pooled trust will accept if you have assets other than cash.

C. Third Party Trusts

Third party special needs trusts are funded with assets belonging to someone other than the beneficiary. Unlike the self-settled trusts discussed above, these trusts are not specifically authorized by statute. These trusts can be established by the third party during their lifetime (inter vivos) or upon their death through their last will and testament (testamentary). Third party trusts are frequently used by parents who have a child with a disability.

Third party trusts do not have a Medicaid payback requirement. Thus, upon the death of the beneficiary, remaining trust assets can be distributed as directed in the trust, such as to other heirs of the person who funded the trust. To maintain the trust's exemption from Medicaid payback, it is very important that the trust funds not be mixed with a first party trust. If third party funds are co-mingled with first party funds, ALL of the trust funds will be subject to a payback requirement. Third party trusts also do not have an age requirement for establishment.

[9] *See* 42 U.S.C. §1396p(d)(4)(C)(iv).

Third party trusts help a disabled person maintain eligibility for public benefits because the assets owned by the trust are not considered resources of the beneficiary until actually paid out for the benefit of the beneficiary. At the time of payment, they are treated as income for the beneficiary. Because of this, it is recommended that payments should not be paid directly to the beneficiary, but to vendors benefitting the individual. Additionally, because SSI recipients are automatically eligible for Medicaid in Georgia, it is imperative that distributions not violate SSI rules by providing "food and shelter" and that the trustee be educated on the In-kind Support and Maintenance ("ISM") rules of SSI.

D. Other Trust Types

In addition to the three main types of special needs trusts discussed above, another type of trust that may be used for benefits planning is the Miller trust, also known as a Qualified Income Trust. A Miller trust is established to protect the eligibility of benefits such as Medicaid for a beneficiary who otherwise exceeds an income cap for such benefits.[10] Excess income is transferred or channeled into the trust and used to satisfy the patient liability. This type of trust is considered self-settled, thus there must be a provision for Medicaid payback at the beneficiary's death. Miller trusts are frequently used for a client who needs nursing home Medicaid, but receives monthly income, such as social security or pension income, that is above the maximum limit to qualify for Medicaid.

III. Who can be the Beneficiary

Self-settled d4A trusts must be established and funded before the beneficiary reaches the age of 65.[11] An individual may add to the trust after obtaining the age of 65, under certain circumstances. However, this is only allowable if the trust contains the irrevocable assignment of the right to receive payments from an annuity or support payments created before the trust

[10] 42 U.S.C. §1396p(d)(4)B).
[11] 42 U.S.C. §1396p(d)(4); GEORGIA MEDICAID MANUAL §2346.

beneficiary reached the age of 65.[12] Continuing such annuity or support payments are paid to a special needs trust and are treated the same as payments made before the individual attained age 65, which do not disqualify the trust from the special needs trust exception.

If the beneficiary is age 65 or older, they may be able to use a d4C pooled trust; however, in Georgia, the beneficiary would incur a transfer penalty for the transfer of assets that may interfere with Medicaid benefits.[13]

Self-settled trusts must be distributed for the sole benefit of the beneficiary.[14] This means that any distributions from the trust for services or goods must be for the beneficiary's benefit, not for the benefit of others. For example, the trust may purchase event tickets for the disabled beneficiary, and even a companion if necessary for assistance, but the trust cannot purchase event tickets for the beneficiary's entire family.

The funds in a third party trust were never the beneficiary's assets and therefore are not subject to many of the same restrictions as self-settled trusts, such as the sole beneficiary rule or payback provisions. Third party trusts can have multiple beneficiaries and there are no restrictions on who can be the remainder beneficiary or beneficiaries. The funds remaining in a third party trust at the disabled beneficiary's death are treated just like a regular estate plan.

IV. Distributions from a Special Needs Trust

Despite what type of trust you choose, it is important to remember that the pure existence of the trust does not protect the beneficiary. To adequately protect the beneficiary, funds from the trust must be distributed in such a way that does not disrupt the beneficiary's benefits. Limiting expenditures by the trustee is critical to comply with SSI and Medicaid benefits and income restrictions. Distributions must be made to supplement but not replace the public benefits.

[12] POMS SI 01120.203.B.1.c.
[13] GEORGIA MEDICAID MANUAL §2342.
[14] 42 U.S.C. §1396p(d)(4); GEORGIA MEDICAID MANUAL §2346.

The restrictions placed on distributions and expenditures from the trustee depend on the type of benefits the beneficiary is receiving. This is why it is critical for the trustee to have a clear understanding of what assistance the beneficiary is currently receiving or may need in the future; and be familiar with SSI restrictions regarding ISM and food and shelter expenditures.

Georgia's Department of Community Health requires an annual accounting be submitted to show the expenditures made on behalf of the beneficiary. Violations of the ISM or food and shelter rules could result in retroactive ineligibility of means tested benefits such as SSI.

A. Resources and Income

If the beneficiary is on any public benefit that is "means tested", such as SSI, it is very important that the trust not make any distributions to the beneficiary that would cause the beneficiary's countable resources or income to exceed the maximum allowable for eligibility. This also requires close attention to what is considered a countable resource or income.

"Income" for public benefits is not the same as "income" for tax purpose or even what you think of as "income". A good rule to keep in mind is *if it can be converted to cash, it **is** income*. To prevent the beneficiary from having excess income, the Trustee should never distribute cash directly to the beneficiary; nor should the Trustee distribute directly to the beneficiary: **anything that can be converted to cash**. Distributions are usually paid directly to third party vendors that provide goods and services to the beneficiary. Furthermore, if income is distributed to the beneficiary, and not spent in the same calendar month it is received, the income becomes a countable resource the following month.

Recipients of SSI and Medicaid must report any changes in income, resources, and living arrangements to the Social Security Administration and the Department of Family and Children Services. Creation and funding of a special needs trust must be reported as a change in income and resource. Reporting does not mean that the Special Needs Trust will automatically be considered a resource or income; however, failure to report may result in penalties to the beneficiary.

B. In-kind Support and Maintenance

In-kind support and maintenance is also generally considered countable income for means tested benefits. In-kind support and maintenance arises when another person pays for or contributes to a recipient's food or shelter expenses.[15] Distributions from a special needs trust for food or shelter, even if paid to a third party vendor on behalf of the beneficiary, may reduce the beneficiary's SSI income. Thus in general, distributions from the Special Needs Trust should be for items OTHER THAN food or shelter for SSI recipients. There are situations where it is in the beneficiary's best interest to provide food or shelter items, but that is beyond the scope of this paper.

In-kind support and maintenance distributions include payments toward:

- Food
- Rent
- Room and board
- Mortgage and property insurance required by the lender
- Property taxes
- Utilities such as gas, electric, water, sewer, and garbage collection

The following are generally NOT considered in-kind support and maintenance:

- Renter's insurance or Fire insurance
- HOA dues
- Renovations or improvements to a home to make it accessible for the disabled individual
- Cable television or internet subscription services

[15] 20 C.F.R. §416.1130(b).

C. Common Expenditures

Common expenditures from a special needs trust include payments to third party vendors for the following services or items:

- Durable medical equipment
- Personal care services
- Educational expenses
- Transportation expenses
- Cable television or entertainment expenses
- Dry cleaning and laundry services
- Entertainment such as tickets to cultural or sporting events
- Items or services not covered by Medicaid

V. DRAFTING TIPS

When drafting a Special Needs Trust, pay careful attention to the following basic requirements:

A. Make the Trust Irrevocable

In order for a special needs trust to be excluded as an asset or resource of the beneficiary, **the trust must be irrevocable**. This means that the grantor cannot make any changes once the trust has been created and only the Trustee controls the money or other property owned by the trust. In Georgia, all trusts are presumed to be irrevocable unless the trust specifically reserves the power of the grantor to revoke or modify the trust.[16] However, a careful drafter will expressly state that the trust is irrevocable and the grantor retains no power to revoke or modify the trust.

To avoid unintended consequences or to address unforeseen circumstances, the trust should be drafted so as to allow the trustee or trust protector to amend the trust in response to unforeseen circumstances or changes in eligibility requirements.

[16] O.C.G.A. §53-12-40.

B. Sole Benefit Rule

Self-settled trusts must include a provision that all distributions will be made **for the sole benefit of the disabled beneficiary**.[17] Inclusion of this language would be sufficient for the trust to satisfy this requirement, however a careful drafter will include additional restrictions so that the trustee is not induced to violate the sole benefit rule.

C. Spendthrift Status

In Georgia, a trust must prohibit both voluntary and involuntary transfers to qualify as a spendthrift trust. It is sufficient for the trust to include a term that the beneficiary's interest is subject to a spendthrift trust.[18] A spendthrift trust protects assets against most creditors. However, a spendthrift provision is unenforceable against the following types of claims: alimony; child support; taxes; tort judgments; judgments for restitution arising from the criminal conviction of the beneficiary; or judgments for necessaries such as food, housing, and medical bills.[19]

D. Income and Principal or Corpus

The trust should clearly identify what will be allocated to income versus principal. This is especially important if the trust will receive capital gains. By Georgia statute, a trustee shall allocate to principal: money received from a sale, and realized profit from an exchange in assets.[20]

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[17] 42 U.S.C. §1396p(d)(4); GEORGIA MEDICAID MANUAL §2346.
[18] O.C.G.A. §53-12-80(b).
[19] O.C.G.A. §53-12-80(d).
[20] O.C.G.A. §53-12-420(2).

E. Trustee Discretion for Distributions

Delineating trustee discretion in the terms of the trust can be tricky. Too liberal discretion may frustrate the purpose of the trust and language stating that the trustee can only supplement benefits may be too restrictive for the beneficiary's particular situation. In order to maximize the benefit of the trust to the beneficiary and properly limit the trustee's discretion, the trust should include terms directing that the assets and income of the trust are to "Supplement not Supplant" any public benefits received by the beneficiary. However, the terms should also allow flexibility in spending to maximize the beneficiary's quality of life so long as it does not interfere with or extinguish benefits. Even if allowed by the Trust document, a trustee must understand whether the beneficiary is receiving SSI and what distributions would be considered ISM and therefore reduce the monthly SSI amount paid to the beneficiary and potentially causing termination of Medicaid benefits.

F. Trust Protector

Including a trust protector in a special needs trust helps insure that the trust will be managed and distributed properly. A trust protector can step in if a trustee is making distributions that risk the eligibility of a beneficiary for public benefits. A trust protector may also be used to revise the trust without filing a court petition. This is important in order to maintain compliance with ever-changing Medicaid rules. The trust should include language stating that the purpose of trust is to maintain the beneficiary's public benefits and the purpose of trust protector is to revise the trust for compliance with Medicaid and other public benefits.

Care should be given when drafting powers given to a trust protector. The trust protector should not be given so many powers that they become a co-trustee. Not only can expansive powers create friction with the trustee, but may also impose a fiduciary duty on the trust protector that may not have been intended. It is advisable that the trust state that the trust protector is NOT a trustee and owes no fiduciary duties to anybody or has any duty to act. However, it is prudent to note that the declaration of no fiduciary duty is not enough to make it so – the trust protector must act in a limited manner to avoid a fiduciary duty being imposed on the position.

It is recommended that the trust protector be someone who would be considered an independent trustee, and not a descendant of the trust beneficiary. It is not uncommon for a family to have no one that would be willing or able to serve as a trust protector. In that case, it is recommended that the trust protector provisions be included in the trust along with some language regarding the selection of a trust protector such as reserving the right to nominate a trust protector at a later time or upon a specific event, or directing a specific person to appoint a trust protector at such time as one is necessary.

Legal Ethics

Submitted by Charles M. Hall

LEGAL ETHICS

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Unless you have been brain dead for a while, then you recognize that lawyers, as a group, don't fare well in the public mind, and that we have reputations that make us the butt of jokes, sometimes with justification, but usually, because people seem to love to hate lawyers. That is, until they need one.

Lawyers are widely seen as:

(1) making a lot of money;

(2) being dishonest;

(3) being unscrupulous;

(4) blood suckers;

(5) if not totally dishonest, then at least distorters of the truth; and/or

(6) hired guns.

This list, of course, isn't exhaustive or exclusive to lawyers or necessarily directly on topic, but given our bad reputations, which, I believe, is largely undeserved and in many cases, flows directly from the public's misunderstanding of our adversarial system of justice and dispute resolution system, and the fact that the law is not black and white, but involves shades of grey, every lawyer has a duty not to add to the public's dim view of the profession, by avoiding those things that cross the line between what our profession is allowed to do and what is not permitted.

With that in mind, our self-regulating State Bar has been kind enough to adopt a lengthy set of rules known as the Georgia Rules of Professional Conduct, which can be found on-line at the State Bar website, generally:

(http://www.gabar.org/barrules/ethicsandprofessionalism/index.cfm)

and more specifically at:

http://www.gabar.org/barrules/georgia-rules-of-professional-conduct.cfm

Most of the rules really don't need much explanation as to why they have been adopted although their meanings may be in doubt and I am sure that all of us have consulted some of them, if not on a regular basis, then at least when (1) another attorney does something that sounds or looks questionable; (2) a client, opposing counsel or opposing party has threatened to file a bar complaint; (3) an actual bar complaint has been filed; or (4) a client has asked us to do something that just doesn't sound right It is the later that is most applicable to this paper.

The Bar does maintain a "help line" (**404-527-8741 or 800-682-9806)** that a lawyer can use to get advice or help when an ethical question arises, but from my own experience, what usually happens is that you will be directed to the rules, and probably even to a specific rule, and left to figure it out for yourself. I don't say this as a criticism of the Bar, however, because I learned a long time ago that our rules of conduct, just like a most of the law we deal with, are not bright lines, but rather are capable of interpretation, except of course, when it comes to your escrow account. Except for that, and getting convicted of a crime of moral turpitude that directly reflects on your honesty and trustworthiness, most of us have to rely on seminars like these to figure out what to not to do.

Answers can also be obtained to questions submitted on-line, using your member log-in.

Who is Your Client?

When being asked to draft a trust, the obvious answer to "who is your client" is that, at least to begin with, your client is the grantor or at least, that should be the answer. However, because a trust has beneficiaries, which might include the grantor and others, the definition of client should probably be expanded to include the third-party beneficiaries, including the contingent beneficiaries.

While a direct attorney-client relationship will not exist between the attorney and the non-grantor beneficiaries, the rules that apply to the attorney-client relationship that are found in the Georgia Rules of Professional Conduct that all Georgia lawyers are bound by will probably also apply, in most cases, to the indirect relationship between the attorney and the third-party beneficiaries. One should remember that if the attorney has screwed up, it probably won't do any good for the attorney to claim that the client is dead and that the unhappy beneficiaries are owed no duty whatsoever. It will also not be much of a defense to a malpractice action.

The issue of who your client is also may come up when a third-party has initiated the meeting and has brought the client in for the purpose of making a trust or a will with a trust.

It is important to identify your client so that you can avoid conflicts and so that you know to whom you owe the duties that Rules of Professional Conduct spell out.

An attorney has a duty to avoid compromising situations involving a client, since those situations have a strong tendency to affect the attorney's ability to provide unbiased advice to the client. One thing that may come up and that could be described as a compromising situation, is where the grantor asks the attorney to be the trustee. In my opinion, unless you are an immediate family member drafting the trust at the request of the grantor (like one or more of your parents), this is a request that should be denied. The obvious thing that comes to mind is that it will be difficult to avoid the ugly allegation that you have a conflict of interest, no matter how much the grantor trusts you and no matter how honest you think you can be and after the grantor has left the scene, you will be left open to the justified or unjustified claims of the beneficiaries.

If enough money is involved, disgruntled beneficiaries will search far and wide for someone to blame. An example that is currently being played out involves the Rollins family.

http://www.forbes.com/sites/clareoconnor/2014/09/29/inside-the-3-billion-feud-tearing-georgias-rollins-family-apart/#652113ed38ab

So far the attorneys in the Rollins family saga are not the target and probably won't be, since this is a family squabble and the trustee(s) are the sons of O. Wayne Rollins and one "independent trustee."

While the Rollins trustees probably only have their reputations to consider, having a lawyer who participated in the drafting of the complicated scheme of multiple and related trusts serve as trust, would add a layer of complication, especially since the lawyer has more to lose than his or her reputation.

My strong recommendation is that an attorney who drafts a trust for a client should never agree to serve as trustee, unless the grantor is a very close family member and even then the attorney should think long and hard about it before saying yes. If an attorney who drafts a trust instrument for a grantor agrees to serve as trustee, the attorney should recommend to the client that everything be reviewed by another attorney who can give the client independent advice. If anything goes wrong, the trustee-attorney is open to claims by beneficiaries that may end up affecting the attorney's ability to practice law, including a claim that leads to disbarment. In addition, multiple trustees may help insulate the attorney trustee, but as noted above, if enough money is involved, then the attorney trustee can be expected to be dragged in to the litigation.

An attorney serving as a trustee of a trust he or she drafted at the request of the grantor is going to have a difficult time arguing that he or she did not have a conflict of interest, if something goes wrong. In the Rollins litigation, the dispute is between generations of the same family, but the independent Trustee, who is eighty-eight and was a friend and associate Rollins senior, is still a party to the litigation.

The lawyer who is asked to become a trustee, or who volunteers to be a trustee, may also be compromised by the fact that he or she can earn substantial fees once the trust is established and funded. While these fees are set by statute, they could be substantial.

The Rules of Professional Conduct have several specific rules related to conflicts of interest and what they are and what we shouldn't do, but, like most things written by lawyers and even worse, like most things written by lawyers for lawyers, at least in the rules themselves, little guidance is offered on how to avoid conflicts of interest. Portions of two of these rules are relevant to this topic.

These is a general rule, Rule 1.7 – Conflicts of Interest: General Rule, which says:

“(a) A lawyer shall not represent or continue to represent a client if there is a significant risk that the lawyer's own interests or the lawyer's duties to another client, a former client, or a third person will materially and adversely affect the representation of the client, except as permitted in (b).

(b) If client consent is permissible a lawyer may represent a client notwithstanding a significant risk of material and adverse effect if each affected or former client consents, preferably in writing, to the representation after:

(1) consultation with the lawyer,

(2) having received in writing reasonable and adequate information about the material risks of the representation, and

(3) having been given the opportunity to consult with independent counsel.

. . . “

The difficulty for the lawyer serving as a trustee is that some of the beneficiaries may not even exist yet, so it will be hard to get their consent.

There is also a more specific rule, <u>Rule 1.8 - Conflicts of Interest: Prohibited Transactions</u>, which says:

(a) A lawyer shall neither enter into a business transaction with a client if the client expects the lawyer to exercise the lawyer's professional judgment therein for the protection of the client, nor shall the lawyer knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

(1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client;

(2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and

(3) the client consents in writing thereto.
(b) A lawyer shall not use information gained in the professional relationship with a client to the disadvantage of the client unless the client consents after consultation, except as allowed in Rule 1.6.

(c) A lawyer shall not prepare an instrument giving the lawyer or a person related to the lawyer as parent, child, sibling, or spouse any substantial gift from a client, including a testamentary gift, except where the client is related to the donee.

. . . "

There is language in this rule that could prove troublesome for the lawyer-trustee, if something goes wrong or even if something doesn't go wrong, but beneficiaries complain about decisions the lawyer-trustee makes, since while the grantor may have been happy with the lawyer earning trustee fees (which in the case of a billion dollar trust can be a lot of money), the disgruntled beneficiaries may not be so happy.

The issue that arises where a third-party has brought the grantor client to the lawyer will be discussed below. In those cases it may be more difficult for the lawyer to identify the client in the transaction. Commons sense usually dictates that that the client will always be the grantor, but this can get murky if the lawyer has a previous professional relationship with the client escort and the client escort has contacted the lawyer and asked the lawyer to prepare a document for the "escortee." This will be the case where the person bringing the lawyer and client together is a care-taker or relative who benefits from the trust to a greater degree than other beneficiaries or other similarly situated beneficiaries.

One final thought applies to this situation. If either the person who is doing the escorting or the putative grantor are unknown to you ask for picture identification and make a copy of that identification.

Confidentiality in Third Party Communications

If the trust is created by a Will, its terms are going to be a matter of public record and the lawyer's duty of confidentiality is relieved somewhat, at least as to the terms of Trust. However, all communications between the client and the attorney are subject to Rule 1.6 Confidentiality of Information. (See Appendix I)

And generally, the attorney is bound to preserve the confidentiality of the communications between the attorney and the client, unless relieved of that burden by the client or some other waiver of the privilege, even after the client dies.

The confidentiality of the communications between the lawyer and the client may be compromised altogether if someone other than a member of the lawyer's staff is present while the lawyer and client are communicating, but even in those cases, the lawyer is not given free rein in revealing client confidences, because the privilege belongs to the client.

This gets tricky, since in many cases, the original client may have died before the trust comes into existence, and while the privilege generally survives the death of the client, the lawyer who drafted the trust may have to reveal confidential communications (1) to insure that the intent of the grantor is carried out; (2) in defense of attempts by a beneficiary to defeat the trust (or Will); (3) where the expressed intent of the grantor is to defraud his or her creditors (as opposed to protecting assets from future creditors); (4)

where the grantor is attempting to secrete money from a crime victim; or (5) to respond to bar complaints and malpractice claims made by the beneficiaries against the lawyer.

Certainly, while the client is alive, the lawyer has a duty not to tell a potential beneficiary that his grandmother thinks he is a worthless jerk and therefore he shouldn't be looking forward to an inheritance or enjoying the fruits of a trust fund, unless of course, Grandmother authorizes the attorney to reveal the information as an object lesson to her worthless grandson in hopes that he will mend his ways.

Assessing the Client's Capacity

The Rules of Professional Conduct also have a provision that requires the attorney to assess the client's mental capacity in connection with decisions the client is making that translate into instructions for the attorney.

The rule, Rule 1.14 Client Under a Disability (See Appendix I) places a duty on the lawyer to make some determination regarding whether a client's ability to make a decision is impaired by age, mental or medical disability or for some other reason. The lawyer is still required to maintain a normal attorney-client relationship, but in some cases, the attorney may have a duty to seek the appointment of a guardian or take other protective action (the rule does not say what action) if the attorney believes that the client cannot adequately act in the client's own interest.

For the trust lawyer this might come into play when a client, who is not a regular client, or who is not anyone the lawyer has ever seen before, is brought in by third-party with a request that the lawyer draft a trust or a will with trust provisions.

Not every situation like this is going to be a problem, but where the third-party initiated the appointment and brought the client to the attorney and where the third party is (a) a caretaker; (b) a child, but not the only child; (c) a close relative, but not the only close relative; (d) a neighbor; or (e) a friend, the attorney needs to be alert and should take steps to make sure that what the attorney is being asked to do is what the client wants and what the client understands.

In a situation like this, the attorney should insist on interviewing the client outside of the presence of the person who brought the client in, to assess, as best the lawyer can, the client's capacity to make reasoned and rational decisions, free from the influence of others.

Some red flags might include (a) a request to draft an instrument that favors a caretaker, (b) a request to draft an instrument creating a trust that favor's someone like Anna Nicole Smith (but only where the grantor is very old and drooling); (c) a request that an instrument be drafted that favors one child over all others, or even excludes all children save one; (d) a request that the attorney draft an instrument that favors someone who would not normally be a "natural object" of the grantor's affection; or (e) a request to draft an instrument that raises an attorney's suspicions.

Most of these situations can be investigated by a private discussion with the client and the attorney has a duty to question the client about the source of the request, the client's knowledge of what he or she is doing, the reasons for omitting some children and not others, the client's knowledge of his or her affairs and estate, and anything else that might shed some light on the client's capacity. These are also things that will apply equally to wills and trusts. Once the attorney is satisfied that what the attorney is being asked to prepare is what the client wants, and not something that someone else who is exercising influence over the client wants, the attorney has probably satisfied his or her duty to assess the client's capacity.

Since an intervivos trust can pass assets to successor beneficiaries without anyone having to go to probate court, the lawyer has to be especially alert to schemes that involve undue influence or lack of mental capacity on the part of the grantor.

<u>Avoiding Fraudulent Transfers</u>

In order to be alert to potential fraudulent transfers, the attorney needs to know the basic elements of such a transfer. You will be happy to know that Georgia has adopted the "Uniform Fraudulent Transfers Act" and you can find it at O.C.G.A. §18-2-70, *et. seq.*

A fraudulent transfer as opposed to a perfectly legitimate transfer has several elements, <u>all</u> of which have to be present for the transfer to be voidable.

First, the transfer is one that is made for less than fair market value or adequate consideration and certainly can include one that is made for no consideration at all. A transfer of assets into a trust without anything being received in return would certainly fit into this category;

Second, the transfer has to be for all or substantially all of the transferors assets, leaving the transferor insolvent;

Third, the transfer has to have been made after a claim by a creditor has arisen (such as a judgment) or even after a lawsuit is pending; and

Fourth, while not exactly spelled out in the code, the transfer has to be for some reason that is not legitimate, and probably is being made to hide or protect assets from creditors.

There is also a question of intent, and if the transferor or grantor has no intention of cheating his or her creditors and continues to pay his or her creditors, the transfer is probably not fraudulent, even if the grantor is unable to pay his or her creditors at some later date.

The Act also contains specific rules regarding setting aside the transfer and in some instances piercing the entity that received the property, like a trust.

Where a potential grantor is asking the attorney to place all of his or her assets into a trust, the attorney has a duty to make some inquiries to satisfy himself or herself that he or she is not being asked to help the grantor commit fraud.

The attorney-client privilege applies and the potential grantor should be assured that everything being communicated is protected, because, the attorney wants (hopes) for a candid discussion with the client.

If the proposed transfer has all of the elements set out above and it is to a revocable trust, it won't be very effective anyway, because transfers to revocable trusts do not insulate the property transferred from creditor claims whether or not they are fraudulent. O.C.G.A. §53-12-82.

For these reasons, the attorney has a duty to advise the client that his or her scheme probably won't work and will in fact end up costing more in the end, because he or she will have to pay the creditor's attorney's fees and maybe even punitive damages.

For a more specific definition of a fraudulent transfer found in the act, see O.C.G.A. §18-2-75. Intent is discussed at O.C.G.A. §18-2-74 and insolvency at O.C.G.A. §18-2-72. There is also an exception for good faith or *bona fide* transferees, but if the transferee is a trust created by the grantor, this exception is not going to apply.

The grantor can do all of the things outlined above and it will not be a fraudulent transfer if there is no pending creditor claim, i.e., even if the transfer renders the grantor "insolvent" since a debt free grantor can hardly be shown to be cheating non-existent creditors.

In other words, it may be possible to place ones assets into an irrevocable trust, with a spendthrift clause, if there are no pending claims and the intent is not to defeat or cheat creditors, but rather the intent is to protect the grantor's property from an impending descent into dementia or from the fear that grantor might be going into a business venture that could result in ruinous liability claims, like real estate development (i.e., future, not yet identified claims). The problem of course, is that the trust has to be irrevocable, which means that the grantor is giving up some or all of the control.

Where the grantor is trying to protect his property or assets from potential future creditors, Georgia does not make it easy and because the grantor forfeits a large measure of control, trusts set up for this purpose in Georgia are not very common.

Obviously, the attorney has a duty to avoid helping the client avoid making fraudulent transfers, if for no other reason, than to avoid the grantor filing a third-party complaint against the attorney, when the grantor gets sued by the creditor. In addition, and because fraud is such an ugly word, the attorney who is asked to participate in a scheme to defraud a client's creditors should politely decline and send the client away, after the appropriate lecture of course. Willfully participating in a fraudulent scheme may be illegal and might cost an attorney his or her license.

And it is probably not a good idea to refer the client to a less scrupulous colleague or at least a colleague you think is less scrupulous.

That said transferring assets into a trust to defeat creditors, even current creditors is probably better than what one of my current clients did (before he came to see me, of course.) A client heard, while attending a professional meeting, that a good way to keep your property away from potential creditors was to transfer it to your children. In this case, that is exactly what the client did. Unfortunately the children were minors and subsequent events intervened to really foul things up. To say that the situation appeared to FUBAR[1] is a considerable understatement. The property was ultimately lost.

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[1]For the exact meaning use Google or ask a Marine.

APPENDIX I

SOME BAR RULES

RULE 1.1 COMPETENCE

> A lawyer shall provide competent representation to a client. Competent representation as used in this Rule means that a lawyer shall not handle a matter which the lawyer knows or should know to be beyond the lawyer's level of competence without associating another lawyer who the original lawyer reasonably believes to be competent to handle the matter in question. Competence requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

The maximum penalty for a violation of this Rule is disbarment.

RULE 1.6 CONFIDENTIALITY OF INFORMATION

a. A lawyer shall maintain in confidence all information gained in the professional relationship with a client, including information which the client has requested to be held inviolate or the disclosure of which would be embarrassing or would likely be detrimental to the client, unless the client gives informed consent, except for disclosures that are impliedly authorized in order to carry out the representation, or are required by these Rules or other law, or by order of the Court.

b.

1. A lawyer may reveal information covered by paragraph (a) which the lawyer reasonably believes necessary:

i. to avoid or prevent harm or substantial financial loss to another as a result of client criminal conduct or third party criminal conduct clearly in violation of the law;

ii. to prevent serious injury or death not otherwise covered by subparagraph (i) above;

iii. to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client;

iv. to secure legal advice about the lawyer's compliance with these Rules.

2. In a situation described in paragraph (b)(1), if the client has acted at the time the lawyer learns of the threat of harm or loss to a victim, use or disclosure is permissible only if the harm or loss has not yet occurred.

3. Before using or disclosing information pursuant to paragraph (b)(1), if feasible, the lawyer must make a good faith effort to persuade the client either not to act or, if the client has already acted, to warn the victim.

c. The lawyer may, where the law does not otherwise require, reveal information to which the duty of confidentiality does not apply under paragraph (b) without being subjected to disciplinary proceedings.

d. The lawyer shall reveal information under paragraph (b) as the applicable law requires.

e. The duty of confidentiality shall continue after the client-lawyer relationship has terminated.

The maximum penalty for a violation of this Rule is disbarment.

RULE 1.7 CONFLICT OF INTEREST: GENERAL RULE

a. A lawyer shall not represent or continue to represent a client if there is a significant risk that the lawyer's own interests or the lawyer's duties to another client, a former client, or a third person will materially and adversely affect the representation of the client, except as permitted in (b).

b. If client informed consent is permissible a lawyer may represent a client notwithstanding a significant risk of material and adverse effect if each affected client or former client gives informed consent, confirmed in writing, to the representation after:

1. consultation with the lawyer, pursuant to Rule 1.0(c);

2. having received in writing reasonable and adequate information about the material risks of and reasonable available alternatives to the representation, and

3. having been given the opportunity to consult with independent counsel.

c. Client informed consent is not permissible if the representation:

1. is prohibited by law or these Rules;

2. includes the assertion of a claim by one client against another client represented by the lawyer in the same or substantially related proceeding; or

3. involves circumstances rendering it reasonably unlikely that the lawyer will be able to provide adequate representation to one or more of the affected clients.

The maximum penalty for a violation of this Rule is disbarment.

Rule 1.8 Conflicts of Interest: Prohibited Transactions

(a) A lawyer shall neither enter into a business transaction with a client if the client expects the lawyer to exercise the lawyer's professional judgment therein for the protection of the client, nor shall the lawyer knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:

(1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client;

(2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and

(3) the client consents in writing thereto.

(b) A lawyer shall not use information gained in the professional relationship with a client to the disadvantage of the client unless the client consents after consultation, except as allowed in Rule 1.6.

(c) A lawyer shall not prepare an instrument giving the lawyer or a person related to the lawyer as parent, child, sibling, or spouse any substantial gift from a client, including a testamentary gift, except where the client is related to the donee.

The maximum penalty for a violation of Rule 1.8(b) is disbarment.

The maximum penalty for a violation of Rule 1.8(a) and 1.8(c)-(j) is a public reprimand.

RULE 1.14 CLIENT WITH DIMINISHED CAPACITY

a. When a client's capacity to make adequately considered decisions in connection with a representation is diminished, whether because of minority, mental impairment or for some other reason, the lawyer shall, as far as reasonably possible, maintain a normal client-lawyer relationship with the client.

b. When the lawyer reasonably believes that the client has diminished capacity, is at risk of substantial physical, financial or other harm unless action is taken and cannot adequately act in the client's own interest, the lawyer may take reasonably necessary protective action, including consulting with individuals or entities that have the ability to take action to protect the client and, in appropriate cases, seeking the appointment of a guardian ad litem, conservator or guardian.

c. Information relating to the representation of a client with diminished capacity is protected by Rule 1.6. When taking protective action pursuant to paragraph (b), the lawyer is impliedly authorized under Rule 1.6(a) to reveal information about the client, but only to the extent reasonably necessary to protect the client's interests.

The maximum penalty for a violation of this Rule is a public reprimand.

APPENDIX II

<u>Hypothetical Scenario</u>

You are contacted by George Harrison. He wants you to prepare a trust for his mother, who has been ill and may need extended nursing home or assisted living care soon.

You find out the following information George:

(a) Mrs. Harrison is 93 years old;

(b) George has a brother and two sisters;

(c) George has been living with his mother in the house that he and his siblings grew up in and he says that he has been taking care of his mother without any assistance from his siblings;

(d) Mrs. Harrison is a widow;

(e) Mrs. Harrison has the following assets:

(1) unencumbered real estate valued at $1,000,000.00;

(2) an investment account with a reputable brokerage firm, valued at $1,250.000.00 as of the end of the prior month;

(3) jewelry insured for $250,000.00;

(4) 100 ounces of gold bullion in a safe in her home; and

(5) and a monthly income from social security, a pension and a 401(k) left to her by her late husband Dr. Harrison that averages about $10,000.00 each month.

(f) Mrs. Harrison is disappointed in all of her children, except for George and she has loaned all of them money, but never received a penny of repayment and they never come to see her;

(g) Mrs. Harrison has a day-time aide who helps her with dressing, eating and getting to and from the toilet;

(h) Mrs. Harrison is not ambulatory; and

(i) George has a written, durable financial power of attorney given to him by his mother that gives him complete authority to act on her behalf.

George wants you to prepare an irrevocable Trust, naming him as Trustee and his mother as beneficiary. He tells you that his mother wants to transfer all of her assets to a the Trust, to protect them, that she is to receive the income from the trust, including from the 401k, pension and social security and that on her death, everything in the Trust should be split between George and two charities (501(c) (3) type entities, selected by the Trustee.

George tells you that his mother is very ill and that she cannot get out of the house and he wants you to prepare the trust and all of the transfer documents so that assets can be transferred. He wants you to provide detailed written instructions and he will take the documents and get them executed and witnessed. He also wants you to get a tax identification number for the trust.

George will also pay you a flat fee of $15,000.00.

<u>Should take on the assignment?</u>

(1) Who is your client?

According to George, your client would be his mother, but is George your client?

(2) If Mrs. Harrison is your client, how do you evaluate her capacity?

(3) Does it matter if George has a durable power of attorney?

(4) Do any of you smell a day old dead flounder anywhere in this?

(5) What are your ethical considerations?

(a) Without a chance to talk to Mrs. Harrison, you only have George's word that his mother wants to "disinherit" his siblings;

(b) Even if George has a durable power of attorney does his fiduciary duty prevent unilateral action on his part?

(c) Being a careful attorney, you have a chance to perform some due diligence, as you check out title to the assets and discover a judgment against George and his mother from Bentley Credit Corporation for $175,000.00, and the judgment was recorded three days before George came to see you;

(i) Does this create a problem?

<u>What should you tell George?</u>

<u>What if you run into one of George's siblings in Church and that sibling asks if you are doing some legal work for George or Mrs. Harrison. Can you say anything?</u>

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