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A Primer on U.S. "Death" Taxes: An Accurate Description or a Political Perspective?

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ABSTRACT
This paper discusses issues relating to estate and inheritance taxes that may be owed to both the federal and state governments as a result of the dearth of a decedent. The paper begins with a brief overview of the requirements of a valid will and outlines the probate process. It then turns to an in-depth discussion of issues relating to estate taxation and strategies that might be utilized to minimize any liabilities and taxes owed either by the estate or by an individual beneficiary.

Key Words: Valid Will; Undue Influence; Estate and Gift Taxes; Trusts; Unified Credit

INTRODUCTION: SOME BASICS

Death can be both a personal as well as a financial tragedy. In the United States, as elsewhere, the death of a spouse, partner, mother or father, or other relative or friend can bring a host of issues to the forefront. Arranging for the burial of a person is traumatic; arranging to settle an estate in terms of marshaling assets, paying debts, and then distributing the assets of a decedent carries with it additional burdens and responsibilities. One of these burdens is to understand the potential taxability of the decedent's estate or of individual beneficiaries for estate and inheritance taxes. In addition, it is important to understand select strategies that can be employed to minimize the impact of taxes on an estate—more specifically through the creation of a trust.

For many years, I have said to my students, "A will is a document that purports to pass property at death time." This is a good place to start. A valid will is a legal document that expresses the choices of a testator or testatrix [testator/trix] *how* property is to be disbursed and *to whom* it should be transferred upon the death of the testator/trix (see generally Crawford, 2019). For many people, the will also sets forth the person or persons who would assume responsibility for the care and custody of any minor children. There are several types of wills.

- A *testamentary will* is the traditional document that is signed, notarized, and includes the attestation of witnesses. A testamentary will is also called a *statutory will* (Uniform Probate Code, Section 2-502(a)(1), 2008).
- An *oral or nuncupative will has not been reduced to writing*, but is expressed verbally by the testator/trix in the presence of witnesses. Some refer to an oral will as a "soldier's and sailor's will," since many of these wills were created on a battlefield when there was no time to create a more formal will. Another name for an oral or nuncupative will is a "deathbed will, "referring to the testator speaking his bequests and his wishes to witnesses, usually because he has no opportunity to make a written will" (Bird, 2019, p. 1). Many states and the Uniform Probate Code do not accept the validity of an oral will (Crawford, 2019, p. 281, citing Uniform Probate Code Section 2-502(a)(1)). Bird (2019, p. 1) notes that only "11 states accept nuncupative, or oral, wills under certain

circumstances: Florida, Indiana, Kansas, Mississippi, New York, North Carolina, Ohio, Tennessee, Texas and Vermont. The state of Washington also accepts them, but only from members of the United States military." In most states that accept an oral or nuncupative will, the witnesses must reduce the oral will to a writing and the testator/trix must actually die as a result of the event or circumstance that prompted the oral testament.

Interestingly, a *video* will be considered (if at all) under the same criteria as an oral or nuncupative will. In addition, states that require that a will be in writing will sometimes accept a video will but only if it is accompanied by a written will (generally Mandel, 2018).

- A *holographic* will is found "entirely in the handwriting of the testator/trix" and does not carry with it the requirement of any witnesses (Cheung, 2018a; Jackson, 2019).
- A *living will* is does not actually involve the transfer of property. Instead, a living will provides directives as to what should happen if a person becomes incapacitated and can not make medical or financial decisions on their own behalf. A living will often provides for a Medical Power of Attorney or an Advanced Directive, or instructions for burial or cremation (Fine, 2019).

Requirements of a Valid Will

This article provides a context by citing detailed examples of the legal requirements of a valid for illustrative and comparative purposes from the state of California and the state of New Jersey. [See the Legal Notes in Appendix I.] The state of California provides a general description of the requirements for a *Last Will and Testament* in its comprehensive Probate Code. At the outset, it should be understood, however, that most states will also accept a will that was executed in another state if the document is valid under that state's law, thus avoiding the requirement that a new will must be executed each time a testator/trix changes their residence to a different state.

According to the California Probate Code (see Appendix I), the general requirements for a valid will are as follows:

(a) the document must be written (meaning typed or printed);
(b) the document must be signed by the person making the will (the "testator/trix"); and
(c) the document must be attested to by two witnesses who were present to witness the execution of the document by the maker and who also witnessed each other sign the document.

In California, as in most other states, any person eighteen (18) or more years of age who is of sound mind may make a will (Harkness, 2018). "Sound mind" generally means someone who has not been deemed incompetent by a court in a prior legal proceeding (see *In re William W. Bassford*, 2019; Quinnipiac Probate Law Journal, 2019).

If a testator/trix is unable to physically sign his or her name, he or she may direct another party to sign the document on their behalf. The will may also be signed by a conservator (a guardian and protector appointed by a judge to protect and manage the financial affairs and/or the person's daily life due to physical or mental limitations or old age), again, pursuant to an order of a court. Each witness must either see the testator/trix sign the will or be told by the testator/trix that the signature on the will is his/hers; must understand that the document is the testator/trix's will; and must sign the will in the testator/trix's presence and in the presence of the other witness. This is referred to as the "process of attestation." Witnesses, however, do not have to read the will itself or know of the contents of the will (generally Cheung, 2018b).

Witnesses to a will must be *competent*. In addition, in order to avoid any potential difficulties, the witnesses to the will should be "*disinterested*," which means that a witness is not a beneficiary under the will. If a witness is not "disinterested" in that sense, it may create a presumption that the witness procured the gift by "duress, menace, fraud, or undue influence." If a gift fails because the witness is not able to rebut the presumption, in many cases by "clear and convincing evidence" (Pardo, 2013; Siefker, 2019), the interested witness will forfeit the portion of the gift that exceeds the value of any gift they would have received if the testator had died intestate. Pardo (2013, p. 604) notes that "For the clear-and-convincing standard, the explanation must be substantially better than the alternatives." In other cases, the "interested" witness will forfeit all gifts made to him or her in the will.

The Issue of Undue Influence

In many jurisdictions, the presumption of undue influence is created with the introduction of evidence which would establish (1) the existence of a confidential or fiduciary relationship between the grantor and a fiduciary party, (2) the fiduciary or the interest he or she represents benefits from the transaction, and (3) the fiduciary had an opportunity to influence the grantor's decision in that transaction. It appears that the confidential relationship is the "linchpin of the undue influence inquiry" (Madoff, 1997; see also *In re Mortimore*, 2012; *In re Teller's Estate*, 1939; *Donovan v. Bromley*, 1897).

As a second example, the state of New Jersey (see Appendix I) has established the legal requirements for making or "executing" a valid will:

- A person executing a will must be at least 18 years old;
- He or she must be "of sound mind." (Sound mind generally means someone who has not been deemed incompetent by a court in a prior legal proceeding);
- A will must be in writing (New Jersey does not recognize an "oral will");
- A will must be signed by the testator/trix and attested to (witnessed) by two persons who witnessed the testator sign the will, or who witnessed the testator/trix acknowledge his or her signature on the will itself. As in California, if a testator/trix cannot physically sign his or her own name, he or she may direct another party to do so on their behalf.
- The person making the will must be of "sound mind." Generally, in order to meet this requirement, the testator/trix must understand the meaning and purpose of the will, must understand generally "the nature and extent" of his or her property, and must understand generally the "natural objects of his or her bounty," that is, who are the normal or natural heirs of the testator/trix.

The Connecticut Supreme Court discussed the extent of undue influence sufficient to invalidate a will:

> *"the degree of influence necessary to be exerted over the mind of the testator to render it improper, must from some cause or by some means be such as to induce him to act contrary to his wishes, and to make a different will and disposition of his estate from what he would have done if left entirely to his own discretion and judgment. That his free agency and independence must have been overcome, and that he must, by some dominion or control exercised over his mind, have been constrained to do what was against his will, and what he was unable to refuse and too weak to resist" (Lee v. Horrigan, 1953).*

Distler (2019, p. 131) stated that "Emerging laws authorizing electronic estate planning documents, remote notarization and electronic signing processes, could increase the opportunity for undue influence."

The fact that the testator/trix has a mental disability that prevents him or her from understanding the purpose of a will, or if the testator/trix is suffering from dementia (Purser & Lonie, 2019) and does not generally know the extent of his or her property, might raise an issue regarding that person's competency to execute a valid will.

In determining the "nature and extent" of property of a decedent, certain assets are not included in the "estate" of a decedent, such as the proceeds from life insurance policies (unless the proceeds are made payable to an estate), community property (community property is income or property acquired by a husband or wife during the course of their marriage, except for the income or property obtained solely by one of them by gift or inheritance), any assets placed in a living or *inter vivos* trust (discussed below), and certain retirement assets held with a designated beneficiary.

Probate

In order to carry out the intentions of the testator/testatrix, the will is required to be submitted to a special court, most often referred to as the *Surrogate's Court* or *Probate Court*, in a process called probate. In some rare cases, a person may file a petition contesting the validity of the will by either stating the will is fraudulent, that the decedent was coerced in making the will through "undue influence," or that the decedent was not in a sound state of mind when drafting the will and thus lacked the legal capacity to create the will. This type of suit is called a "will contest" (see, e.g., *In re Guinn's Estate*, 1951).

Renee Hykel Cuddy (2019), writing on *Legal Zoom,* outlines "the four basic steps" of probate:

1. A person, most often the designated executor/trix of the decedent (or sometimes the surviving spouse or child or children) will file a *petition* with the Probate Court and give notice to heirs and beneficiaries. This is sometimes described as the "opening of the estate."
   The Probate Court is asked to either (1) admit the will to probate and appoint the executor/trix, or (2) if there is no will, that is, the decedent has died *intestate*, appoint an administrator/trix for the estate. Generally, notice regarding the petition must be provided to all of the decedent's heirs and beneficiaries. If an heir or beneficiary objects to the petition, they will have the opportunity to do so in court. The notice of the hearing is normally published in a local newspaper in order to attempt to notify others, such as unknown creditors of the decedent, of the commencement of the proceedings.
2. Following appointment by the court, the personal representative must *give notice* to all known creditors of the estate and take an *inventory* of the estate property based upon the requirements of state law. A creditor who wishes to make a claim on assets of the estate must do so within a limited period of time, which also varies by state.
   In taking an inventory, the personal representative must include all of the decedent's probate property, including real property, stocks, bonds, business interests, and any other assets. In some states, a court appointed appraiser will be required to value the assets—especially if there is a question regarding the value of any individual asset.
3. All estate taxes, any expenses of the decedent's "last illness," funeral expenses, and debts must be paid from the estate.
   The personal representative must determine which creditor's claims are legitimate and pay those and any other final bills from the estate. In some cases, the personal representative will be permitted to sell estate assets to satisfy the decedent's legal obligations and debts.
4. Legal title in property is transferred according to the will or under the laws of intestacy (if the decedent did not have a valid will).

> Following a required statutory waiting period designed to allow creditors to file claims against the estate, and after all legitimate claims and bills are paid, the personal representative will petition the court for the authority to transfer the remaining assets to beneficiaries as directed in the decedent's Last Will and Testament; or, if there is no valid will, the remaining assets will be distributed according to the state's Law of Intestate Succession. If the will provides for the creation of a testamentary or trust, as described below, money is then transferred to the trustee. Unless the beneficiaries of the estate waive the requirement, the petition may include an accounting of how the assets were managed during the probate process. Once the petition is granted, the personal representative will create new deeds for property, transfer stock to the proper beneficiary, liquidate or sell off assets, and transfer other designated property to the appropriate beneficiaries (adapted from Cuddy, 2019).

According to *Inheritance Funding* (2019), "When a resident of New Jersey dies, the New Jersey probate courts oversee the distribution of all assets and belongings left behind. They first appoint a representative to be in charge of the estate, collect and itemize all assets and monetary accounts, ensure all outstanding debts are paid off, and determine the validity of any existing wills. Finally, when the court is satisfied that all other steps have been completed, they authorize the distribution of inheritance funds to the rightful heirs."

TAXATION ISSUES

This year alone, nearly three million Americans will die. Issues relating to taxation of their estates are important and must be carefully considered and planned for by the individual and their families alike. The process today is carried out through estate planning—often accomplished with the assistance of an estate panning professional (Jones, 2018; Baxter, 2018). This primer is designed to offer a basic understanding of the important concepts and vocabulary involved in the estate planning process.

The Estate Tax

There are generally two ways to die (legally). One is with a valid will, which is called dying *testate*. The second is dying without a valid will, which is called dying *intestate*. Generally speaking, if a person dies testate, they will appoint the person (or persons) to carry out the intentions expressed in the will. In addition, with a few exceptions, the testator/trix will determine to whom their property will be given. Agbo (2019) commented that adults have the "right and absolute freedom to bequeath or devise their properties to persons or institutions of their choice as they wished in Wills without let or hindrance. They could go to the extent of disinheriting family members and dependants." While the context of Agbo's comments was the common law of England and the Wills Act of 1837, the same is equally true in the United States. Exceptions to this principle are cases involving a "pretermitted" or "forgotten" heir (Storrow, 2019) and the ability of a spouse to "elect against the will" and to take a forced or statutory share under certain circumstances (Storrow, 2019).

If a person dies intestate, the court will appoint a party to act as the personal representative of the individual who has died. If a party dies without a valid will, the estate will be distributed according to the rules of intestacy or under the terms of the Law of Intestate Succession, and not according to the legally unexpressed intentions of the decedent (see, e.g., Andrews, 2018).

Estimates indicate that more than $1 trillion in wealth changes hands in inheritance and gifts each year. The estate tax is a tax imposed on the total value of a decedent's estate at the time of their death. Opponents of the tax, most notably former Alaskan Governor Sarah Palin, frequently referred to the estate as a "death tax." In the sense that it is imposed only at the decedent's death, Ms. Palin was correct. The estate tax may be imposed by either or both the federal government or by a state government. Whether or not an estate tax return must be filed by the decedent's executor/trix or their court appointed administrator/trix will depend on the *taxable value* of an estate. For estates above the threshold amount, only the amounts that exceed the threshold amount for that year are taxable.

Due to what is termed as the *marital deduction* (Chaffin, 2019), the transfer of assets to a surviving spouse is not taxable, and only assets transferred to other heirs may be taxable (Baxter, 2018). The marital deduction was an important issue in the United States Supreme Court's recognition of "same sex" marriage (*Obergefell v. Hodges*, 2014), where in one case the plaintiff had argued that the inability to be considered married under federal law precluded the consideration of the marital deduction and thus was a violation of her right to "equal protection" under the Fourteenth Amendment to the U.S. Constitution (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2509443Calabresi & Begley, 2014; Herzig, 2014; Schmid, 2015).

As a factual matter, according to data supplied by the Tax Policy Center (2019) at the Urban-Brookings Institute, most Americans ultimately do not pay the estate tax. In 2017, 3,780 estates owe the estate tax. In those cases, the "effective" tax rate, which is defined as the percentage of the estate's value that is paid in taxes – was an average 16.6 percent.

The Estate Tax and Federal Tax Revenues

As a point of reference, the Center on Budget and Policy Priorities (2019) reported that in fiscal year 2018, the federal government raised over $3.3 trillion of its $4.1 trillion budget. Borrowing financed the remaining amount ($779 billion)—future taxpayers will ultimately pay this deficit as a part of the national debt. They wrote:

> *"Half of all federal revenue (51 percent) comes from individual income taxes. The income tax is generally progressive: higher-income households pay a larger share of their income in income taxes than lower-income households do.*
> *Another 35 percent of revenue comes from payroll taxes, which are assessed on the wage or salary paychecks of almost all workers and are used to fund Social Security, Medicare Hospital Insurance, and unemployment insurance. By law, employers and employees split the cost of payroll taxes, but research has shown that employers pass their portion of the cost on to workers in the form of lower wages.*
> *Payroll taxes as a whole are regressive: they collect a higher percentage of total earnings from lower-income workers than higher-income ones. However, if one looks at the overall impact of Social Security, Medicare, and unemployment insurance — the benefits they provide as well as the taxes they collect — these programs are progressive.*
> *Corporate income taxes make up about 6 percent of federal revenue, with the remaining 8 percent coming from excise taxes, estate taxes, and other revenue sources. Excise taxes are collected on the sale of certain goods (e.g., fuel, alcohol, and tobacco); they are intended to raise revenue and, in some cases, discourage consumption of the taxed product. These made up about 3 percent of federal receipts in 2018.*
> *The estate tax is a tax on assets such as cash, real estate, or stock that are transferred from deceased persons to their heirs. Because the first $22.4 million of a married couple's estate was exempt from the estate tax in 2018, and due to other special exemptions from the estate tax, fewer than 1 of every 1,000 estates owed the estate tax in 2018. Because it affects only those who are most able to pay, the estate tax is the most progressive component of a tax code. Estate tax revenues made up 0.7 percent of total federal receipts in 2018."*

The federal government no longer relies on the estate tax and the gift tax discussed below as a major source of revenue. Lundeen (2015) reported that "In 2014, the estate tax raised $19.3 billion according to the OMB, or 0.6 percent of total federal revenue of over $3 trillion. Estate tax revenue has dwindled in recent years. Its share of total revenue is down from about 1 percent in 1990." Huang and Cho noted "Today, 99.8 percent of estates owe no estate tax at all, according to the Joint Committee on Taxation. Only the estates of the wealthiest 0.2 percent of Americans — roughly 2 out of every 1,000 people who die — owe any estate tax. This is because of the tax's high exemption amount, which has jumped from $650,000 per person in 2001 to $5.49 million per person in 2017."

The effective rate of taxation is low for several reasons. As explained above, the main reason is that the estate tax is imposed only on the portion of the estate *above* the exemption. Secondly, the estate tax is literally riddled with legal "loopholes" or exceptions that permit taxpayers to shield portions of their wealth from the government (Alaska Bar Rag, 2019). A major loophole permits parents "sell" parts or all of their assets to their children, often at an amount far below the fair market value. Another major way to avoid or significantly reduce the estate tax is through the creation of a trust.

The Inheritance Tax

The major difference between an estate tax and inheritance tax is *who pays the tax.* The inheritance tax is a tax imposed by a state and not the federal government. In normal circumstances, the estate of a deceased will be passed onto their heirs. (One exception occurs where the deceased literally has no heirs. In this case, the estate will *escheat* to the state (DeRosa, 1997; Hirsch, 2004). Unlike the estate tax which is paid by the estate, an inheritance tax is usually paid by the *person inheriting an estate*. The estate tax is imposed based on the decedent's estate before the proceeds are distributed to any beneficiaries (Jones, 1987). The level of taxation applied is dependent on the *relationship* between the decedent and the heir, and the *value of the property* received by the heir. In all states, inheritance from a spouse or domestic partner (where this type of legal relationship has been entered into by a same sex couple) is exempt from inheritance taxation. In addition, most children will pay little or no inheritance tax.

VALUING THE ESTATE

An estate consists of the assets, less any liabilities, of a decedent. The term "assets" includes "anything of value," such as cash, securities (stocks and bonds), real estate, insurance, trusts, annuities, and any business interests. The value of an asset is based on its "*fair market value*," which is a "reasonable amount" at which an asset can be purchased by a "ready and willing" buyer in an "arm's length" transaction. (In some cases where there is a difference of opinion among heirs—or the government—an appraisal of the estate may be ordered by the competent Probate Court with jurisdiction over the estate (generally Lennhoff, 2009)). The *gross estate* is the total fair market value of a person's assets. After the fair market value of the assets of a decedent is determined, certain liabilities or reductions may be *deducted* from the gross estate.

The most common of these liabilities or deductions include mortgages, unpaid debts, and the expenses of estate administration. In addition, assets that are passed to a surviving spouse or "qualified charities" are not included in the gross estate. Chen (2018) notes that:

> *"A qualified charitable organization is a nonprofit organization that qualifies for tax-exempt status according to the U.S. Treasury. Qualified charitable organizations include those operated exclusively for religious, charitable, scientific, literary or educational purposes, or the prevention of cruelty to animals or children, or the development of amateur sports. Nonprofit veterans' organizations, fraternal lodge*

groups, cemetery and burial companies, and certain legal corporations can also qualify. Even federal, state and local governments can be considered qualified charitable organizations if the money donated to them is earmarked for charitable causes."

Strategies for Reducing the Estate Tax

There are several ways to reduce estate taxes. As noted above, a taxpayer may decide to make a donation to a qualified 501(c)(3) organization (Hopkins, 1983; Poterba, 2001). There is generally no limit on the amount that can be donated to a qualified charity. An unmarried couple should also consider marriage! If a person dies without a "legal" spouse, the entire estate can potentially be subject to the estate tax. If the decedent is married, all assets will fall under ownership of the surviving spouse, unless otherwise provided in a will or by the operation of law.

Since the inheritance tax is imposed by an individual state, it might also be important to consider the question of residency. Currently, 19 states and the District of Columbia currently impose some form of a *state* estate or inheritance tax. These states are Connecticut, Delaware, Hawaii, Illinois, Iowa, Kentucky, Maine, Maryland, Massachusetts, Minnesota, Nebraska, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, Tennessee, Vermont, and Washington—although the trend appears to be the elimination of state inheritance taxes (Juehring, 2019). The author recently moved to Florida. One consideration was the absence of any state inheritance tax (or state income tax, as well).

GIFT TAXES

The IRS has provided guidance on questions relating to gifts. The Internal Revenue Service (IRS) (2019) notes:

"The gift tax is a tax on the transfer of property by one individual to another while receiving nothing, or less than full value, in return. The tax applies whether the donor intends the transfer to be a gift or not. The gift tax applies to the transfer by gift of any property. You make a gift if you give property (including money), or the use of or income from property, without expecting to receive something of at least equal value in return. If you sell something at less than its full value or if you make an interest-free or reduced-interest loan, you may be making a gift."

The Annual Gift Tax Exclusion

A gift tax exclusion will allow an individual to gift a set amount each year—the amount is $15,000 for 2019—to as many individuals as the donor desires without incurring a gift tax. However, at the point at which more than this amount is gifted to any individual donee, the gift tax will be triggered. As defined by the IRS, a gift can be "anything of value" and may include cash, stocks and bonds or other investments vehicles, real estate, or jewelry. The gift tax exclusion has been adjusted to account for inflation.

Certain categories or types of gifts are exempt from the gift tax. Lenfert (2019) notes that these include gifts to qualified charities (as defined above), gifts to spouses, gifts to political organizations, gifts relating to educational expense concerning tuition that are paid directly to an educational institution (Marmon, 2019), and gifts relating to medical expenses that are paid directly to the medical facility.

What is the "Unified Credit"?

The "unified credit" is a credit for the portion of estate tax due on the taxable estate calculated by the Internal Service Revenue (IRS) in order to combine the federal *gift tax* and *estate tax* into one. The unified credit is intended to prevent a taxpayer from gifting away too much of their assets during their lifetimes in order to avoid the imposition of estate taxes.

According to Willms-O'Leary (2018): "The federal gift and estate tax exemption amount is the amount of assets that a U.S. citizen can give away during life or at death without the imposition of federal gift or estate tax." Any amounts given away by a decedent during life or at death in excess of the exemption amount that do not qualify for a deduction are taxed at a 40% rate.

The 2019 federal gift and estate tax exemption amount is $11,400,000 per individual. A married couple can give away up to $22,800,000, an amount which includes gifts made in prior years in excess of the yearly limitation, without the imposition of gift or estate tax.

If a married individual dies in 2019 and does not use all of his or her exemption amount, a "*portability election*" can be made to transfer the decedent's unused exemption amount to the surviving spouse. As a result, a surviving spouse will have their own exemption amount, plus the unused exemption amount that was transferred to them from the deceased spouse.

Interestingly, unless Congress revisits the issue by 2026, the exemption amount is scheduled to drop to approximately $6,300,000 per person ($12,600,000 per couple).

TRUSTS

In many cases, a trust should be considered in estate planning (Dukeminier & Sitkoff, 2013). A trust is a "fiduciary arrangement that allows a third party, or trustee, to distribute assets according to mutually agreed upon conditions." The Roy Legal Group (2019) notes that "Trusts are established to provide legal protection for the trustor's assets, to make sure those assets are distributed according to the wishes of the trustor, and to save time, reduce paperwork and, in some cases, avoid or reduce inheritance or estate taxes."

The trust document will permit the imposition of conditions relating to the terms under which the assets of the trust will be distributed. A trust can also be used to protect heirs from creditors, and may offer significant tax benefits and protection for the assets of an estate.

There are two types of trusts (Garber, 2019): A testamentary trust is generally created in a will and takes effect upon the death of the testator or trustor. A living trust, which is also called an *inter vivos* trust, is created during the grantor's or trustor's lifetime. A major benefit of a living or *inter vivos* trust is that the living trust will allow the transfer of assets to a beneficiary after death without a person having to go through the probate process. On the other hand, a testamentary trust will not protect assets from the probate process since it is dependent on the terms of a will.

Revocable and Irrevocable Trusts

Julia Kagan, writing for *Investopedia* (2019a), notes that "An irrevocable trust is a type of trust where its terms cannot be modified, amended or terminated without the permission of the grantor's named beneficiary or beneficiaries." The grantor generally cannot act as trustee and manage the trust's assets.

One of the reasons for setting up an irrevocable trust relates to estate and tax considerations. Since an irrevocable trust removes all incidents of ownership from the grantor, it effectively removes the assets of the trust assets from the grantor's (also called the settlor) taxable estate. In addition, the grantor does not have any tax liability on the income that the trust generate. The trust is responsible for the payment of any income taxes.

Irrevocable trusts may be especially attractive to certain professionals such as doctors or lawyers. As a matter of law, once property has been transferred to an irrevocable trust, the property is now owned by the trust for the benefit of the named beneficiaries. As such, it is immune from legal judgments and collection actions by creditors of the grantor. On the other hand, revocable trusts do not offer the same protection against legal action or estate taxes as do irrevocable trusts.

Irrevocable trusts come in two forms: living or *inter vivos* trusts and testamentary trusts. Examples of living trust may include: irrevocable life insurance trust; grantor-retained annuity trust (GRAT) (Kagan, 2019b), spousal lifetime access trust (SLAT) (Kitces, 2013), and qualified personal residence trust (QPRT) (Find Law, 2019). In addition, living trusts may include charitable remainder trust and charitable lead trust (both forms of charitable trusts)

Testamentary trusts are by design irrevocable as they are created after the death of the deceased. A testamentary trust is funded from the decedent's estate according to the terms of a will. However, because a will is *ambulatory* and only takes effect upon the death of a testator/trix, the grantor may change or cancel a testamentary trust at any time before his or her death.

As Julia Kagan (2019a) writes in *Investopedia* (2019), "Property transferred to an irrevocable living trust does not count toward the gross value of an estate. Such trusts can be especially helpful in reducing the tax liability of very large estates." When considering revocable trusts, it must be understood that that any property held in one still belongs to the trust's creator and therefore may be included in his or her estate for tax purposes or when qualifying for government benefits such as Medicaid or other forms of assistance which are based on income.

Testamentary trusts are by their nature irrevocable since they are established in the "Last Will and Testament" of the testator/testatrix. Most revocable trusts, on the other hand, can be dissolved (revoked) entirely, allowing for more control on the part of a grantor or trustor.

InvestorWords (2019) notes that a revocable trust is a "trust that may be altered or terminated during the grantor's lifetime. Since the trust may be altered at any time until the grantor's death, it is considered part of the grantor's estate and is subject to taxation. The property is passed on to the beneficiaries only after the grantor's death, and the revocable trust then becomes irrevocable."

There are some negatives attached to creating a revocable trust. In many cases, there may be significant "upfront costs" involved. On the other hand, the beneficiary of an irrevocable testamentary trust will be able to avoid costs associated with the probate of the decedent's last will. In setting up and funding a revocable trust it will be necessary to arrange for asset transfers from sources such as banks or other financial institutions which can be time consuming and somewhat cumbersome in many cases.

CONCLUDING COMMENTS

I remember hearing from my own grandfather when I was very young: "Everyone is going to die—and I may too!" What should be quite obvious that death and estate planning are very difficult topics for discussion—and even more so for action. While it is important for the layman to understand the basic concepts and vocabulary of gifting, wills, estates, and trusts, only a professional estate planner can guide an individual to make the right choices. The implications of tax planning are so obvious—and so fraught with danger—that only in combination with a person of specific competence will the layman be assured that the right choices have been made (Baxter, 2018). This paper is designed to impart that basic understanding of these important topics so that any individual can communicate effectively with the professional he or she has chosen to assist in making the proper decisions for their future.

APPENDIX I: LEGAL NOTE

In California, the laws regarding the valid execution and witnessing of a Will are set forth in the California Probate Code; Division 6 Wills and Intestate Succession; Part 1 Wills; Chapter 1 General Provisions Section 6100; Chapter 2 Execution of Wills, Sections 6110 & 6112; and, Division 7 Administration of Estates of Decedents; Part 2 Opening Estate Administration; Chapter 3 Probate of Will; Article 2 Proof of Will, Section 8220.

In New Jersey, law regarding probating of an estate is found in N.J.S.A. 3B:3-22 et seq. The law regarding the validity of a wlll in N.J.S.A. 3B, Section 3-1, et seq.

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