<u>Fact Pattern No. 3</u>: Art and Lynn Andrews

Dear Mr. and Mrs. Andrews, this memorandum is intended to memorialize and confirm information received from you during our meeting earlier this month, to describe the current state of your planning and articulate suggestions for the possible update of your planning.

1. Client background: When meeting with you, we learned that you are married and have two children (ages 10 and 11). Art is 40 years old, and Lynn is 39. Art is an engineer employed by a local computer company, and he earns $150,000.00 per year. Lynn is a partner in a law firm with one other attorney. She practices in the area of environmental law, and her partner practices in the area of real estate development. Lynn had net income from her practice last year of $175,000.00.

2. Client Assets: Your estate consists of the following assets (after liabilities):

- residence: $1,250,000.00
- 401(k) plan benefits: $250,000.00
- Roth IRA: $ 30,000.00
- stocks and bonds: $100,000.00
- cash and savings: $ 100,000.00
- miscellaneous personal property: $ 20,000.00
- interest in law partnership: $500,000.00

You have a mortgage of $850,000.00 (secured against your residence), you owe $75,000.00 to Lynn's parents (incurred in starting the law partnership), and you have $10,000.00 in credit card debt.

You stated that due to Lynn's income, you believe that you will be able to pay off the debt to her parents within the next 3 years to 5 years, and that you can then start saving an increased amount of money for your retirement and your children's education.

Lynn is a sole child, and she expects to receive an inheritance from her parents at their death of approximately $5 million. Her parents are in their early seventies, but they are not in the best of health.

Art's family has limited financial resources, and little inheritance is expected from them.

Lynn is concerned about liability for debts, and liabilities incurred by the partnership and her partner. They have $1 million in malpractice insurance, but she is concerned that this is not enough and is afraid of a judgment that could wipe out any potential inheritance.

3. Client Goals: Your estate planning goals include the following:

a. You wish to prepare an estate plan, as from the information received, none is currently in place.

b. You wish to pay off the debt to Lynn's parents in the next three (3) years to five (5) years, and then start saving an increased amount of money for your retirement and your children's education.

c. In doing so, you wish to make certain that your children's college education is paid.

d. In addition, you wish for any moneys are to go to the children to be held for them until they reach age 30, at which time they can have one-half of the funds held for them, and the remainder of these funds can be given to them when they reach age 35.

e. The youngest of your children, Jeff, has some learning disabilities that may require special education and additional expenses, for which planning should be in place.

f. The expenses anticipated with Jeff will not be incurred in educating your other child, Sally, and this should be addressed.

g. You would like asset protection for your property, due to Lynn's law partnership and law practice.

4. Existing Planning. As stated above, from the information received, no existing planning is in place.

5. Issues to consider:

a. Existing Planning. No existing planning is in place. Given your assets, liabilities, and being the parents of two (2) children, it is highly recommended that you make estate plans. No preference as to who might serve as guardians for your minor children (if you could not) has been indicated by you, and so thought should be given to this issue. Moreover, generally, existing estate planning should be reviewed periodically (every two (2) to five (5) years and with every major life event, for example, the death of a family member and the birth of a family member). Moreover, to avoid a potential conservatorship / guardianship, it is always recommended that a power of attorney be in place. Further, it is critical that your family know what medical care you would like. For example, do you want life savings measures or life support? Therefore, a health care poxy and living will, and HIPAA Release be in place for each of you, in the event of incapacity and/or a medical emergency. And to make certain that it is respected by third parties, the Power of Attorney should not be more than two (2) years old.

b. Asset Protection.

From the information provided, many or most of your assets are titled in your individual names. Moreover, while your Roth IRA is regulated under the Employee Retirement Income Security Act ("ERISA"), unlike a 401(k), it is not a qualified plan under Federal law. As such, asset protection for your Roth IRA is governed by state law, and in California, your Roth IRA may be seized by creditors. California law shields funds in IRAs and Roth IRAs that are considered necessary to support the owner (and the owner's dependents) during retirement taking into account all resources that are likely to be available for support, but any surplus may be collected by creditors. The further the owner is from retirement age, the less likely funds may be considered necessary for support in retirement. But, that determination is left to a Court in the event of a creditor action. See Code Civ. Proc. §704.115(e). For this purpose, rollover of a 401(k) into an IRA is not advisable for asset protection purposes.

It is important how title to your residence is held. Is it held as tenancy-by-the entirety (a joint-tenancy for married couples)? Or is it held in Art's or Lynn's name alone? This is a critical issue, as the greatest creditor protection is afforded by tenancy-by-the-entirety, which can only exist between married spouses. Neither spouse holds an individual share of the tenancy-by-the-entirety property, and therefore tenancy-by-the-entirety property may not be used to satisfy either spouse's individual debts. A creditor typically would have to have a claim against both spouses on the same cause of action to reach the tenancy-by-the-entirety property, or the tenancy would have to be set aside for fraud.

Title to bank and investment accounts should be reviewed, given Lynn's liability concerns. To the extent accounts are titled in her name or in a joint tenancy with Lynn, they could be attached by her creditors. Or, with a joint tenancy, property might go to the "wrong person", that is, the person with creditors.

What is the "corporate" structure of Lynn's law practice? A general partnership should be avoided, as each partner is liable for the acts of the other partner. Or is it instead a professional corporation, professional limited liability partnership, or a professional limited liability company, which is recommended? This is of critical importance, given Lynn's liability concerns. Moreover, to the extent available, professional liability insurance should be obtained – as much as can be obtained and reasonably afforded.

What type of liability insurance do you have, if any? Do you have an umbrella policy?

c. Probate in California.

While providing a thorough process in California, you may wish your estate to avoid probate for several reasons, including that a typical probate proceeding may last 9 to 24 months, it can be costly due to probate fees being based on the gross value of the probate estate and the fee amounts (which are based on statutory law), and the process being subject to public disclosure. These are considerations in a decision whether to utilize last will and testament-based planning or revocable living trust-based planning (and seeking to avoid probate).

Generally, you can accomplish the same goals with either type of planning (that is, last will and testament-based planning or revocable living trust-based planning). However, if fully funded, a revocable living trust-based plan can permit the avoidance of probate. It may also arguably better facilitate disability planning and the update of your planning.

d. General Due diligence. The following questions should be answered, and appropriate action taken.

a. Do you have an updated schedule of assets, fully detailing the above described asset information, including

i. for your bank and brokerage accounts, (i) the type of account, (ii) the name of institution, its location and relevant account number(s), (iii) in who's name the account(s) is(are) held, and (iv) the approximate value(s) of each account; and

ii. for stocks, bonds, and mutual funds, (i) the number of shares / face value of bond(s), (ii) a description, (iii) in who's name the account is held, and (iv) the approximate value(s) of each; and

iii. for retirement assets, (i) a description of the account / institution, (ii) the current beneficiary designation, and (iii) the current beneficiary designation and the approximate balance of each asset?

b. As indicated above, how are all of your assets titled? Jointly" Individually? If individually, in whose name?

c. As indicated above, are your beneficiary designation forms completed, and up to date? For your life insurance, your 401(k) plan benefits, and your Roth IRA?

d. Are any of your accounts held with a transfer at death or payable at death designation and direction, including your investment accounts and your bank account(s)? If the designated beneficiary predeceased you, will this still accomplish your planning goals?

e. Are any of your assets titled as a joint tenancy?

f. As to any assets held as a joint tenancy, does your joint tenant have any creditor concerns? If the joint tenant predeceased you, will it still accomplish your planning goals? Has this caused any gift tax consequences?

g. What type of life insurance policy(ies) do you own? For each, who is the insurance company, what is the policy's face amount, who is the owner, the insured, and the beneficiary? Does it have any cash surrender value, and have any loans been taken against it?

h. As indicated above, who are the designated beneficiaries of your life insurance policy, and are your beneficiary designations up to date?

i. A description of your tangible personal property (household furnishings, artwork, jewelry, collections, silver, and more). To whom do you wish to leave any specific special assets, for example, your wedding dress, wedding ring, and the like?

j. A description of any other significant or "special" assets, including interests in any lawsuit, copyrights, patents, mineral rights, and more.

k. Information on any gifts previously given, including information on the date, recipient, a description of the gift, and its value.

e. <u>Estate Tax Concerns</u>.

i. <u>Background</u>. As a background, the estate tax is a tax on your right to transfer property at your death. Your estate consists of everything you own or have certain interests in on the date of death (including the value of all property over which you hold a general power of appointment, or, if within three (3) years of the time of death, the value of such property when such power was relinquished during lifetime). The fair market value of these items constitutes your taxable "gross estate."

With estate planning, there are four (4) types of taxes to consider, (i) the estate and gift tax, (ii) the generation skipping tax, (iii) income tax, and (iv) the real property tax consequences of your actions.

Given your net value ($2,250,000), your estate is not subject to an estate tax. However, you anticipate increased assets in the future as you save and with Lynn's anticipated inheritance, and so this should be monitored. Moreover, the currently increased exemption amount of $11,700,000 for 2021 (with an annual gift tax exclusion of $15,000 per grantee) is temporary, and it is scheduled to sunset, or revert, to $5 million per person (adjusted for inflation) as of January 1, 2026. That said, it may be reduced before then, and to a lesser number.

A primary goals of marital trust planning is to defer until the second death or, potentially, completely avoid the estate tax by use of the lifetime exemption amount at the first death. This is accomplished by keeping the two (2) estates separate from each other by use of irrevocable living trusts, and utilization of the lifetime applicable exclusion ($11,700,000 for 2021) to the fullest extent possible. [IRC §2056 requires use of the marital deduction for property transferred to the surviving spouse.] Moreover, please note that IRC §1014(b)(6) provides for a basis adjustment of one hundred (100%) percent of community property, thereby causing a basis-adjustments for both spouses' shares at the first death, which is helpful for income tax planning (capital gains planning) purposes.

The following options are generally available with marital planning.

All to the Surviving Spouse, outright or in trust. This option is the simplest, with everything left to the surviving spouse (either outright or in trust). With this option, the surviving spouse generally has full control over the trust property left to him or her, and he or she may later change his or her planning by amending the trust through a general power of appointment.

The Marital Disclaimer Trust Approach. A second option is "disclaimer trust" planning to pass all assets to the surviving spouse (outright or in trust) but reserve an option for the surviving spouse to disclaim all or a portion of the decedent's share into a bypass trust (aka B trust or family trust). A disclaimer is a refusal by someone to accept property that he or she is otherwise due to receive. The person signs a disclaimer, making an irrevocable and unqualified decision to refuse any interest in the disclaimed property, which must comply with Federal and state law. The disclaimer must be made, and the disclaimed property must be transferred to, the bypass trust not later than nine months following the death of the first spouse.

This is a common form of "wait and see" approach for some married couples, which also can help guarantee that their children will eventually inherit (by making them the ultimate beneficiaries of the bypass trust). The bypass trust is typically drafted so that the surviving spouse manages it as trustee and has access to income and principal. It can therefore provide a safety net for the surviving spouse, if the surviving spouse needs more funds, but creditor protection too, as the surviving spouse does not "own" the disclaimed assets. That said, access to principal must be limited to the ascertainable standards, for example, 5 x 5 powers[9] or health,

[9] A right to the greater of $5,000 or 5% of the trust assets.

education, maintenance, and support (the "HEMS" standard), and it might also be made subject to an exhaustion clause. Under IRC §2041, the HEMS standard is the primary exception to a general power of appointment (which would cause inclusion of assets in the bypass trust in the survivor's gross estate when he or she dies).

The above said, if the surviving spouse appoints a third-party independent trustee over the bypass trust, the trust may contain a broader, non-ascertainable distribution standard (broader than the HEMS standard), and this can further increase the asset protection for the bypass trust.

Assets that are not likely to appreciate may be the best selection for those to be disclaimed into the bypass trust, for capital gains planning. That said, if the survivor's estate might be taxable, you will not want to increase it by adding appreciating assets or requiring income distributions (as per a marital trust). However, as indicated, a "wait and see" (at least until the first death) is possible with this type of planning.

Mandatory Funding Approaches. A third option is to divide the decedent spouse's estate into an A trust and a B trust through various marital deduction funding formulas (commonly known as A/B/C trust planning). Generally, there are three (3) types of marital deduction formula clauses that are used: (i) a Pecuniary Marital; (ii) a Pecuniary Bypass; and (iii) a Fractional Share Formula.

With pecuniary planning, you first determine a dollar amount based on the size of the estate and the size of the available lifetime exemption amount. With funding, you must be careful to not trigger realization of Kenan gain, by not funding the bequest with appreciated assets.[10] Any devise and funding of a pecuniary amount with appreciated assets will trigger recognition and taxable gain. Instead, you will want to fund with assets that have not appreciated in value. Conversely, funding the bypass trust with appreciated assets will not trigger Kenan gain. That said, each approach divides the decedent's estate into shares at his or her death, often creating a share covered by all or part of the decedent's applicable exclusion amount, and another share (or shares) covered by the unlimited marital deduction. Because these are mandatory funding formulas, the surviving spouse must divide the trust according to the formula at the death of the first spouse.

The primary difference between the Pecuniary Marital Trust and the Pecuniary Bypass Trust is where the appreciate and depreciation will end up, in the survivor's trust or the bypass trust. Further, with a Pecuniary Marital Trust, whoever receives the money (Q-TIP Trust or survivor outright) pays the tax. With a Pecuniary Bypass Trust, the bypass trust pays the tax on the appreciating asset (appreciation between the date of death and the date of distribution).

Pecuniary Marital Formula Clause – On the death of the first spouse, the surviving spouse is given exactly enough to avoid tax on the first death, and then everything else goes to the bypass trust. You fund the survivor's side first, with all appreciation going to the bypass

[10] A distribution of appreciated non-cash assets by a fiduciary in satisfaction of a pecuniary obligation triggers realization of gain (capital gain) by a trust or estate. See IRC §663(a)(1) and Kenan v. Comr., 114 F.2d 217 (2d Cir. 1940).

trust. All assets that appreciate are in the bypass trust, and all asset that decrease in value are in the bypass trust. However, you will not know the amount to avoid a tax until you prepare and file an estate tax return. The pecuniary amount is based on the estate tax return (using date of death values).

There are three (3) types of marital formula clauses, with (as stated) the residue passing to the bypass trust (which gets all appreciation and decrease in value): (i) "Date of Death Value" Pecuniary Marital Formula Clauses; (ii) "Fairly Representative" Pecuniary Marital Formula Clauses; and (iii) "Minimum Worth" Pecuniary Marital Formula Clauses. Rev Proc. 64-19 requires that fair market value be used to value assets at the time of distribution, or if Federal estate tax values are used, that assets which fairly represent post-death appreciation or depreciation of the estate be used to satisfy the marital deduction legacy. That said, the real difference between the three (3) clauses is what happens if there is appreciation or depreciation in asset values from the date of death to the date of distribution, with the "Fairly Representative" Pecuniary Marital Formula Clause intended to be fairly representative of the appreciation of all the estate assets available at the date of distribution and a "Minimum Worth" Pecuniary Marital Formula Clause using the lesser of the Federal estate tax values or the date of distribution values.

<u>Pecuniary Bypass Formula Clause</u> – On the death of the first spouse, the bypass trust is funded with a sufficient pecuniary amount to avoid tax at death, and then everything else goes to the survivor. Here, you know the number to fund as of the date of death (that is, use the exemption amount), and so unlike the pecuniary marital formula clause, you do not need to file an estate tax return (which is necessary with a pecuniary marital formula clause, to know the amount to avoid taxes). You know the values as of the date of death and therefore do not need to do a second valuation of assets, which permits immediate funding.

Once funded into the bypass trust, the assets will then be exempt (and always exempt) from estate taxes. Even if there is later appreciation in their values, this appreciation will not be taxed until there is a taxable event, that is, until the property is sold. Moreover, said appreciation will be taxed at the lower capital gains tax rates, rather than the higher estate tax rates.

<u>Fractional Formula Clause</u> – is very simple. Appreciation and depreciation is allocated between the survivor's trust and the bypass trust by a ratio (that is, a pro rata approach). Further, Kenan gain only applies to a pecuniary clause, not a fractional formula clause, and therefore is not a concern. It is the pecuniary portion funded by appreciated assets which triggers recognition and a taxable event.

As with a pecuniary bypass formula clause, with a fractional formula clause, you need not have a second valuation at the date of distribution. Conversely, as stated above, a second valuation is required for a Pecuniary Marital Clause.

A QTIP Trust. With this strategy, the plan is designed as an A/B/C trust plan, but it allows an independent executor to elect QTIP treatment over all or some of the deceased spouse's assets by an election made on the decedent's 706 estate tax return. Any property of the decedent for which the QTIP election is not made then gets funded to the bypass trust. Assets in the QTIP trust are includible in the surviving spouse's estate at death, receiving a step-up in basis at that time. A QTIP trust is a marital trust designed to provide for the surviving spouse while protecting the deceased's assets for future generations.

A QTIP trust is essentially an A/B trust arrangement that is more restrictive than a typical marital trust. In most A/B trust arrangements, the marital (or A) trust is fully accessible by the surviving spouse. With a QTIP trust, the surviving spouse has limited access to the trust assets. Although your spouse must receive all income from the trust (a requirement to qualify for the marital deduction), he or she is not given the authority to dictate the ultimate disposition of the trust assets and therefore cannot withdraw principal from the trust. [That said, the QTIP trust may be drafted with 5 x 5 powers given to your surviving spouse annually without disqualifying it from the marital deduction.] Upon the death of the surviving spouse, the trust is distributed according to the deceased spouse's instructions. Note, this can guarantee that children inherit the trust assets, even if the surviving spouse remarries and later changes his or her plan. It can also be paired with an exhaustion clause, providing that the survivor cannot withdrawn any principal until his or her survivor's estate is exhausted. By planning this way, you provide a safety net but maximum protections that your children will ultimately inherit.

The bypass trust and the QTIP trust can be drafted to be substantially the same. This way the spouse who dies first can ensure that the remainder beneficiaries of the trust are not later changed (subject to any testamentary power of appointment given to the surviving spouse).

Portability. With non-taxable estates, attention should be directed to income tax planning. In such circumstances, you will want to includable all assets in the survivor's gross estate, to take advantage of the second basis adjustment. Further, the survivor can file a 706 estate tax return and claim portability of the deceased spouse's Unused Exclusion Amount ("DSUEA"). With the option for a portability election on the 706 estate tax return at the death of the first spouse, the exemption can be used by a surviving spouse after the first spouse dies.

But, there are some limitations to relying on portability. The DSUEA amount is fixed. Shifting all assets to the survivor may cause a later estate tax, as the property (and the survivor's estate) may appreciate; but, the survivor's lifetime exemption amount will be going down in the future (2026 or before). Further, it provides no protection that the children will ultimately inherit. Moreover, it should be noted that most states do no permit portability for purposes of state estate tax planning.[11]

The Bypass Trust. Even if there is no estate tax concern, there are still reasons for creating a bypass trust. If the surviving spouse has creditor issues, you will want to lock-up the deceased spouse's assets, in case the survivor's assets are lost. If the survivor is in a high-risk profession, for asset protection purposes, you may want to lock-up the decedent's assets into a bypass trust. The risk of a later remarriage and a blended family is another reason, to make certain that your remainder beneficiaries (your children) ultimately inherit the trust assets. Until Proposition 19 is effective, you may also want to use the bypass trust to keep both $1,000,000 exemption (for property tax purposes) available.

[11] The California estate tax is tied to federal state death tax credit. See CA Rev & Tax §§ 13302; 13411.

ii. Real Property Tax Consequences. It should be noted that a transfer to a revocable living trust is not considered a Change In Ownership (CIO) that will trigger a reassessment of real property. Further, a transfer to a revocable living trust should not disqualify you from eligibility under either IRC §121 (exclusion from capital gains on the sale and purchase of a home) or IRC §1014 (basis adjustment at death).

f. Long-Term Trusteeship. As stated for your children too, given your own young ages, there is the potential for a long-term trusteeship. You will want to select a successor trustee who can serve for the anticipated period of the trusteeship.

g. Long-Term Trusteeship; Separate Shares.

Here, we have a potential long-term trusteeship, given the minor ages of your children. You will want to select a trustee who can serve for the anticipated period of the trusteeship. Moreover, care should be taken in selecting a successor trustee(s). Three (3) options include (1) a from or family member, (2) a professional trustee, and (3) financial institutions with trust departments (for example, Bank of America). You need someone who has good attention to detail, is diligent, can handle the pressure, can handle the details (including making necessary filings, such as tax returns and tax elections), and will be around for the entire period of the trust. While financial institutions may be impersonal and there is a turnover among professionals, they offer the necessary skillset, will be around for the trust term, and are bonded by law – all important considerations. A trusted accountant might also be considered.

When minors are a consideration with planning, the creation of separate shares in the trust for the individual children's benefit is recommended. And you may wish to wait for distributions until the child reaches a certain age, to guard against immaturity. [Here, you have stated your wish to wait for outright distributions until age 35 years old.] Distributions can be discretionary until the child reaches a stated age, with mandatory distributions beginning at the stated age and final distributions at a stated age.

You might also provide for discretionary distributions for "good reasons", such as the purchase of a home or business. Alternatively, there is the possibility that a child might develop a drug or alcohol problem, spendthrift problems, a disability, or attract a significant creditor. Therefore, there are reasons to be careful with requiring mandatory outright distributions to them.

h. Equalization. The goal of an estate plan may concern estate equalization, with a goal to balance the desires of the parents making bequests to certain children and the desire to maintain an equitable value to each child. Where the needs of one child demand greater resources than the needs of another child, lifetime gifts or support might be considered by decreasing the child's inheritance based on the extra provided to him or her. Alternatively, life insurance on one or more parent's life can help equalize the distribution of assets.

i. Special Needs Planning. A Special Needs Trust (SNT) allows for a disabled person to maintain his or her eligibility for public assistance benefits, despite having assets that would otherwise make the person ineligible for those benefits. There are two types of SNTs: First Party and Third Party funded. First party SNTs are funded with assets that belong to the trust beneficiary or to which the beneficiary was legally entitled (e.g., assets from an award or settlement, etc.). A third-party special needs trust can be created and funded with assets belonging to a person other than the trust beneficiary (for example, from his or her parents), and to which the beneficiary never had possession or legal interest. Therefore, third party trusts are not subject to recovery by the Department of Health Care Services (DHCS).

j. Asset Protection Planning. Asset protection is very important to estate planning, as estate planning typically involves transfers of assets (to a revocable living trust or a irrevocable living trust, grantor trust, or business entity). That said, planning for a potential claim is permissible, but not a fraudulent transfer following when a claim (including potential claim) arises – which is not permitted under law.

The number one asset protection planning device is personal liability insurance, to make certain that you have sufficient liability insurance. This includes having an umbrella policy. Most liability claims are under $1,000,000, which insurance can protect against. Umbrella policies are available in the event a liability exceeds the underlying policy amount (for example, $1,000,000 of coverage), and they can be obtained up to the amount of $5,000,000. Because such liability is infrequent, umbrella policies are generally very inexpensive (often only approximately $400 to $500 per year).

Another technique is to put your assets outside of the reach of future creditors, by the creation of an entity and the transfer of assets to the entity. By putting assets into an entity, even with your retention of an interest in the entity, you can protect yourself from both insider creditors and outside creditors. You will only own an interest in the entity (not in the assets of the entity), and therefore creditors may not attach the assets of the entity. In addition to being an asset protection vehicle, as described above, an entity can make valuation discounts possible too.

The above said, your principal residence and vacation home should not be placed into an entity, as an entity cannot have a principal residence or vacation home and is, therefore, not eligible for the IRC §121 exemption against capital gains.

Further, California law does not permit the creation and transfer of assets to a self-settled trusts to hide them from creditors, and the transfer of assets to a revocable living trust leaves the transferred assets subject to the trustmaker's creditors. However, you can create an irrevocable living trust with spendthrift provisions preventing assignment or hypothecation of an interest for the benefit of a third party, for asset protection purposes. Assets transferred to the trust would no longer be owned by you, and the trust beneficiary(ies) will not own the trust assets until they are distributed. Moreover, you can provide or direct the trustee discretion in the face of creditors to not make a distribution (even if required under the terms of the trust), save for child support and spousal obligations. You can also authorize indirect distributions, to pay the beneficiary's bills (for example, mortgage, insurance, and the like), without direct distributions to the beneficiary.

As stated above, while your Rollover IRA is regulated under ERISA, it is not qualified plans under Federal law. As such, the Rollover IRA's creditor protections is governed by state law, and in California, may be seized by creditors. California law shields funds in IRAs and

Roth IRAs that are considered necessary to support the owner and the owner's dependents during retirement, but any surplus may be collected by creditors.

k. College Savings. Section 529 Plan makes available a tax-advantaged savings plan that is exempt from Federal taxes and is designed as a way for families to save for college expenses on behalf of a beneficiary (typically, a child). The moneys from a 529 Plan must be used for qualified education expenses in order to be withdrawn tax-free, with eligible contributions possible up to the annual exemption amount ($15,000 for 2021). Five (5) years of gifts possible at one time (for a total of $75,000 for 2021) is possible, but then additional gifts cannot be made into the plan for the ensuing five-year period without gift tax consequences.

Because Federal law considers contributions to a 529 Plan to be gifts made on behalf of the beneficiary, funds kept in these accounts are not considered part of the donor's estate and (if not part of a fraudulent transfer) are safeguarded from the donor's creditors.

That said, in the case of bankruptcy, creditor protection for Section 529 Plans is provided by Federal law, with significant limitations, under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. This act excludes from property of the estate all contributions deposited toward a Section 529 Plan for a beneficiary who is the child, grandchild, stepchild, or step-grandchild of the debtor, and as long as the deposits were made at least 2 years before the bankruptcy was filed and they do not exceed the maximum amount permitted per beneficiary for the program. If the contributions were made between one and 2 years prior to the bankruptcy filing, Section 529 assets are protected up to $5,000 per beneficiary.

In addition to the Federal bankruptcy protections described above, some states have passed statutes that protect Section 529 Plan assets from judgment creditors' claims brought outside of bankruptcy proceedings. Because Section 529 Plans are not Federally regulated, but instead state regulated, each state can set its own requirements. As stated, some states provide protection of Section 529 Plans from creditors, while others only offer creditor protection if the account is in the child's name (not the donor parent's).[12]

However, California is not one of the states that has passed legislation specifying that Section 529 Plans are protected from the creditors of the beneficiary, contributor, and/or the account owner. As such, while Section 529 Plans provide a tax advantaged means to save for your children's college expenses and some creditor protection, the actual level of creditor protection is uncertain.

l. General Partnership. As stated above, a general partnership should be avoided, as each partner is liable for the acts of the other partner. Instead, Lynn and her partnership should form any of a professional corporation, professional limited liability partnership, or a professional limited liability company, as each will afford her liability protection as against the assets of other "partners". That said, Lynn should obtain professional liability insurance.

[12] For example, New York State will protect all assets in a 529 Plan if the account is owned by the child, but only $10,000 if it is owned by someone else, for example, a parent or grandparent.

m. Life Insurance and Disability Insurance. Life insurance can play in important role in estate planning, by providing funds to pay taxes, increased liquidity, the fuel of now available funds, and more. It can provide needed funds with the death of a primary breadwinner. Moreover, it is received income tax free. However, pursuant to IRC §2042, if owned by the decedent, it will be included in the decedent's gross estate. Disability insurance is also very important. When young, you are more likely to become disabled than die. In such event, not only is the person's income potential impaired, but there is now the cost of caring for a disabled person.

When there is a taxable estate or there may be a taxable estate (given an anticipated increase in the value of assets and/or knowing that the exemption amount will be going down in the future), the creation of an irrevocable life insurance trust ("ILIT") or a gift of the insurance policy to children should be considered. Even if some of your lifetime exemption is used, gifting is a more tax efficient option than leaving the insurance in the owner's gross estate (provides a lower effective tax rate). Further, if an ILIT is created, crummy gifts can be made to qualify the gift as a present interest gifts and thereby qualify for the annual exemption amount, without further reduction in the exemption amount.

n. Planning for digital assets – It is encouraged that you organize and inventory your digital assets, listing your various accounts, usernames, passwords, and personal verification questions necessary to access them, as well as any password necessary to access your personal computer, smart phone, or other hardware devices. You should also consider taking advantage of any legacy access services provided by used platforms (for example, Google, Amazon, and Facebook). And you should consider specifically granting fiduciary powers of administration over your digital assets, and consent to disclosure of the contents of electronic communications to fiduciaries.

o. Advanced Planning. For taxable individuals, once foundational planning is in place (that is, you have a last will and testament or a revocable living trust with a pour-over last will and testament, a power of attorney – general durable or springing, health care proxy and living will, and a HIPAA release), you may wish to utilize valuation discounts, tax freezing, and actual techniques to reduce your net gross estate to below the lifetime exemption amount. As indicated above, these strategies may involve the creation of a business entity(ies) and/or a grantor trust(s).

p. Retirement assets — Retirement assets include qualified plans (401(k) plans and 403(b) plans) that are taxed only when money is withdrawn, at the ordinary income tax rate (not capital gain) as the money deposited was ordinary income. Retirement assets are includable in your taxable estate for estate tax purposes. However, if an estate tax is paid, the beneficiary will receive a deduction for the estate tax amount that is paid, so that these monies are not subject to a double taxation (that is, to an estate tax and then an income tax).

Pursuant to the SECURE Act, a "stretch" is no longer available to your beneficiaries, as was permitted under prior law.

With regard to retirement assets, a first question is whether the asset is an ERISA qualified plan. As stated elsewhere, while IRAs are regulated under ERISA, they are not qualified plans under Federal law. For ERISA qualified plans, there are two (2) types of designated beneficiaries (an individual and a trust meeting certain requirements), with a different set of rules for each. To qualify as a designated beneficiary, the trust (i) must be valid under state law, (ii) must be irrevocable as of the date of the plan participant's death, (iii) must have identifiable beneficiaries as of the year following the plan participant's date of death, and (iv) must have an available copy of the plan. If satisfied, the trust qualifies as a designated beneficiary.

You will want your beneficiaries to be designated beneficiaries. If not a designated beneficiary (an estate or charity), distributions must be made within five (5) years of death.

If an individual, there are three (3) options for distributions – (i) a lump sum distribution, (ii) distributions made in installments but subject to the SECURE Act requirements, and (iii) if the designated beneficiary is a spouse, that person can roll the monies over into his or her own IRA (a spousal rollover IRA) and start all over again with required minimum distribution beginning when the money is distributed to the spouse's plan. [That said, the SECURE Act changed the minimum distributions rules, including when distributions must be started (now, as stated above, by 72 years old).]

By way of background, under the Setting Every Community Up For Retirement Enhancement (the "SECURE Act"), except for Eligible Designated Beneficiaries (the "EDB"), the life expectancy method is no longer the default method for determining required minimum distributions ("RMDs"). The new rules require RMDs to be distributed to non-EDBs beginning at the plan participants death, the EDB's death or the minor child's attaining the age of majority. [Prior to the SECURE Act, the Stretch IRA planning technique to optimally dribble out RMDs over the designated beneficiary's life expectancy, but it is no longer available, and in its place a 10-year (versus life expectancy) pay-out is now required.]

The SECURE Act and its 10-year payout requirement commence once the age of majority (age 18) is reached. Prior to then, the minor child is an EDB and tell majority, using the life expectancy method for the pre-majority.

Importantly, every designated beneficiary (an individual or a qualified trust) other than a spouse, a minor, or a chronically ill or disabled designated beneficiary, must now take out over a ten-year period from the death of the plan participant all monies from the qualified plan. As stated, no "stretch" over the beneficiary's life expectancy is now available, except (i) spouses may still stretch over their life expectancy, (ii) minors must start taking a distribution within ten (10) years of turning the age of 18 years old, and must take out all monies within 10 years (that is, by age 28 years old), and (iii) disabled or chronically ill persons can still get a stretch based on their life expectancy. Moreover, as indicated above, if the beneficiary is a non-designated beneficiary (that is, an estate or a charity), the beneficiary is left with the five-year rule. The biggest issue, therefore, is elimination of the stretch.

In light of the above, you may wish to have a trust as a designated contingent beneficiary, rather than naming your minor children individually. [If an accumulation trust, your successor trustee could make or not make discretionary distributions based on existing conditions, such as whether the child exhibits spendthrift behavior or is susceptible to drugs, unstable marriages or creditors. This is opposed to the conduit trust, which requires the RMDs and other plan distributions to be distributed outright to the child once the child reaches the age of majority. Accumulation trust are preferable to conduit trusts for asset protection purposes.] While moneys must be taken out of the plan within the 10-year period and be subject to tax, they need not be distributed from the trust to the beneficiary. Therefore, use of a discretionary trust can still be utilized for creditor protection and spendthrift protection, and to keep these moneys held until your children reach age 35 years. [Qualifying the trust as a grantor trust under IRC §678, so it is taxed at the beneficiary's tax rate rather than the compressed trust tax rates is recommended.]

6. Recommendations

First, it is recommended that foundational estate planning be put in place, including the naming of guardians for your minor children under a last will and testament. For the reasons described above, we recommend that you make a revocable living trust with a pour-over last will and testament. You can serve as trustee of your trust, but thought should be given as to whether you would like a co-trustee and who should serve as your executor under the pour-over last will and testament. Further, Art's sister is being considered as a successor trustee. That said, given the demands and potential length of the trusteeship, substantial consideration should be given as to who could serve in this capacity, and as a successor executor (if need be). In addition, a general durable power of attorney, healthcare proxy and living will, and HIPAA release are recommended, to plan in the event of your capacity and thereby avoid the need for a conservatorship proceeding. In making these documents, the below-described trust provisions should be considered.

Because from the information provided it appears that there is no present control, spendthrift or blended family issues, in designing your estate plan you might consider preparation of disclaimer trust leaving everything to the survivor. If the survivor disclaims a portion, the disclaimed assets would then be funded into a bypass trust (both frozen in value and protected from the survivor's later arising creditors). The survivor could be a trustee of that trust, but the trustee's access to principle should be governed by ascertainable standards (such as 5 x 5 powers or the HEMS standard), to avoid being construed as a general power of appointment and causing estate inclusion. This could be paired with portability (as need be), to potentially fully utilize the lifetime applicable exclusion amount and fully defer any estate tax.

Another alternative, which we suggest, is to use A/B/C trust planning, using formula clauses to fund the bypass and marital trusts. While a fractional formula clause is very simply, we instead suggest use of a pecuniary bypass formula clause. In such circumstances, as stated above, you fund the bypass trust with enough of a pecuniary amount to avoid tax at death, and then everything else goes to the survivor. Because you will know the number to fund as of the date of death (that is, use the exemption amount), unlike with a pecuniary marital formula clause you do not need to file an estate tax return and no second valuation of assets is necessary (which permits immediate funding). And once funded into the bypass trust, the assets will be exempt (and always exempt) from estate taxes. Even if there is later appreciation in their values, this appreciation will not be taxed until there is a taxable event, that is, until the property is sold. Moreover, said appreciation will be taxed at the lower capital gains tax rates, rather than the higher estate tax rates.

As stated above, even if there is no estate tax concern, there are still reasons for creating a bypass trust. If the surviving spouse has creditor issues, you will want to lock-up the deceased spouse's assets, in case the survivor's assets are lost. If the survivor is in a high-risk profession, for asset protection purposes, you may want to lock-up the decedent's assets into a bypass trust. The risk of a later remarriage and a blended family is another reason, to make certain that your remainder beneficiaries (your children) ultimately inherit the trust assets. Until Proposition 19 is effective, you may also want to use the bypass trust to keep both $1,000,000 exemption (for property tax purposes) available.

The bypass trust planning might be paired with providing for a possible QTIP election for the marital trust. As stated above, this can guarantee that children inherit the trust assets, even if the surviving spouse remarries and later changes his or her plan. It can also be paired with an exhaustion clause, providing that the survivor cannot withdrawn any principal until his or her survivor's estate is exhausted. By planning this way, you provide a safety net for your spouse but maximum protections that your children will ultimately inherit.

With regard to your children, as mentioned above, you will want to designate guardians in each of your Last Will and Testament, in the event something were to happen to you. As education savings is a goal, as you save and your assets increase you might consider establishing and your making contributions to Section 529 Plans. You also mentioned estate equalization as a concern (given the special education and additional expenses that will be incurred educating Jeff that will not be incurred for Sally). The purchaser of life insurance to equalize distributions might be considered, with Sally the beneficiary of an ILIT formed by you. Other means to equalize distributions should be considered too, for example, decreasing the Jeff's future inheritance based on the extra provided to him or her. Because this is generally a sensitive issue, further discussion is suggested.

It is also suggested that Jeff's needs and future needs be discussed further. If special needs planning is a concern, further discussion whether a special needs trust is appropriate is suggested. While you stated your wish for outright distributions to your children at ages 30 years and 35 years, to the extent special needs planning is warranted and eligibility for governmental benefits important, the avoidance of outright distributions (in favor of a discretionary trust) might better meet needs in such circumstances.

To the extent Lynn is comfortable speaking with her parents regarding estate planning (particularly their current health), she might discuss with them gifts to Section 529 Plans (and their even frontloading with 5 years of gifting), which can you take maximum advantage of the annual exemption amount and also qualifies as an exception to the generation-skipping tax. Moreover, to the extent she might inherit a significant amount of money from her parents, given Lynn's asset protection concerns, her parents might consider leaving that in a third-party discretionary trust to protect trust assets from Lynn‘s creditors.

As indicated above, a complete Schedule A of your assets should be prepared. In doing so, all beneficiary designations should be considered and confirmed (retirement assets, life insurance, bank accounts, and more (as applicable), and all payable on death and transfer on death designations. If you beneficiary predeceased you, would you goal and purpose still be accomplishes?

Concerning whom might serve as a successor trustee, Art's sister Ann is a Certified Public Accountant, and so she might have the necessary financial skills. That said, a discussion with her is suggested, to learn if she is prepared for such a responsibility – given the duties required, details involved, the possible length of the trusteeship, and the potential liabilities. Alternatively, a professional trustee or financial institution with a trust department might serve. Either could handle the necessary details (including making necessary filings, such as tax returns and tax elections), and will be around for the entire potential period of the trusteeship, and each is bonded by law.

Assuming you serve as healthcare agent for each other, who would serve as a backup is critical. The person selected should be someone who can make tough emotional decisions, and he or she must be prepared for these responsibilities. The level of communication your agents should have with family members in making decisions should also be considered.

Any transfers of your residence should be carefully assessed, to not cause reassessment of these properties, and which would disqualify from eligibility for an exemption from capital gains under IRC §121. Given Lynn's liability concerns, it is recommended that your residence be owned as a tenancy-by-the entirety or by Art as his separate property. Because of California's community property law, specific steps would need to be taken to transmute the property into separate property. Or you might transfer your residence into a revocable living trust created by Art, which importantly would not disqualify eligibility under either IRC §121 or IRC §1014 or cause a reassessment of the property.

While the exemption amount remains high, you might also consider a transfer of your life insurance to an ILIT, with you retaining no incidence of ownership. Moreover, as stated above, the purchaser of additional life insurance to equalize distributions might meet your goals.

Because your Roth IRA is regulated under ERISA, unlike your 401(k), for asset protection purposes rollover of a 401(k) into an IRA is not advisable.

Moreover, your obtaining additional personal insurance (including an umbrella policy) should be considered. Such insurance would provide potentially needed protection, and at an affordable cost. [And Lynn should obtain the maximum available and affordable professional liability insurance, given the nature and potential liability of her law practice, as an environmental attorney.]

Your articulated concerns with potential liability arising from Lynn's law practice would need to be addressed by different means. A general partnership should be avoided, as each partner is liable for the acts of the other partner. Instead, a professional corporation, professional limited liability partnership, or a professional limited liability company is recommended.

In communicating with you, you informed that there is a pending malpractice suit against Lynn's partner and the law partnership for $2 million for a real estate deal that went awry. Given these circumstances, the form of the "partnership" is of paramount importance. If a general partnership, as stated, Lynn is liable for the acts of her partner. Or if instead a professional corporation, professional limited liability partnership, or a professional limited liability company AND assuming there are no claims against Lynn, only the assets of the law partnership and your investment in it is at risk – your personal assets would not be at risk. Moreover, if the law partnership is a general partnership and Lynn therefore has exposure, any transfer of assets by you might be construed as a fraudulent transfer (that is, a transfer when there is a claim against you – whether involving actual fraud with the intent to hinder, delay or defraud the creditor or constructive fraud made without intent but even so leaving you insolvent). Such a transfer is not permitted. Rather, the transfer can be reversed by a judge under the Uniform Fraudulent Conveyance Act (UFCA), and it can result in criminal penalties (California Penal Code §154). Moreover, it can cause a professional (including a licensed attorney) to lose his or her license.

Given the foregoing, more information is needed, including information on the business structure of Lynn's law practice. Moreover, to the extent available, Lynn should have professional liability insurance.

Despite the above concerns, you informed that the lawsuit is likely to be dismissed. However, Lynn will be receiving her share of a contingency case the firm just settled and her share will be $1,000,000.

To the extent Lynn's law practice has been formed as a type of entity (a professional corporation, professional limited liability partnership, or a professional limited liability company) the fee should be first paid to the entity, where it will be protected from inside creditors, who's recovery is generally limited to the entity's assets that are owned and operated by that entity. Otherwise, the creditor does not have many other options when filing a claim. The creditors of the entity are, for the most part, limited to the remedy of a charging order for distributions, if or when the person or persons with the authority to determine distributions chooses to make one. Moreover, the general partner or manager can retain control over any distributions, and may determine to continually reinvest moneys back into the entity, leaving little or nothing for distributions to the partners, members, or shareholders (as the case may be) – or, effectively, to the creditor. This gives the debtor significant leverage in working out a settlement and, at times, denying the creditor any worthwhile release at all. In addition, under Rev. Rul. 77-137, a creditor who obtains a charging order and an assignment of a limited partnership or LLC economic interest is treated as a partner for tax purposes and must report "phantom income" attributable to such interest.

To the extent distributions are made to Lynn, contributions (if not yet made) can be made to Section 529 Plans for the benefit of Sally and Jeff, and/or if there is concern because of Jeff's special needs, to a third-party special needs trust or discretionary trust for his benefit. This might also provide some added asset protection.

In addition to the foregoing, efforts to retain the separate property nature of this contingency amount and the inheritance Lynn might receive from her parents are recommended. Then, to the extent Lynn predeceases Art, these moneys could be funded into her bypass trust to provide a safety net for Art but protect them from his creditors and safeguard them for eventual receipt by or for Sally and Jeff. To the extent a marital trust is created, a QTIP election should be made available by the trust document.

7. Recommended Trust Provisions

a. Because the trust would survive you, it is recommended that you avoid using the word "revocable" in the name of the trust, as a trust becomes irrevocable upon the trustmaker's death.

b. The effective date of the trust should be immediate, to be effective immediately in the event you became incapacitated, as the trust will provide for you during your lifetime (including during a disability.) This can help avoid the necessity of a conservatorship, by providing provisions for your care.

c. As with a Last Will and Testament, you will want to have: (1) distributive provisions and (2) tax provisions. Who gets what, when, and where? And the tax provisions addressing estate tax (perhaps generation-skipping tax) concerns, and perhaps provisions concerning income tax considerations.

d. It is recommended that the trust identify your children, because not every potential trustee may know who they are, to make easier exercise of the successor trustee's duties.

e. Intentions – Under the California Probate Code, a trustee is required to follow the intentions of the trustmaker. It is therefore helpful and recommended to put into the trust instrument the trustmaker's intentions, particularly any particular wishes.

f. Trustee -- With the revocable living trust, the trustmaker should generally be the trustee until such time as he or she has become incapacitated or has passed away.

g. Successor Trustee -- You should not pick someone just because he or she is a friend or family member. You need someone who has good attention to detail, is diligent, can handle the pressure, can handle the details (including making necessary filings, such as tax returns and tax elections), and will be around for the entire period of the trust. [Note, you have minor children, and so there may be a long-term trusteeship, or a long-term trusteeship in the event of your own disability.] You will need someone ready, willing, and able to manage the trust assets, and who can say "no" when appropriate and not be coerced by beneficiaries.

h. Powers of the Trustee –

i. The powers of the trustee should be broad, to address life changes and changes in the law changes, to permit the trust to grow and change as the trustmaker's life changes. The power to amend and revoke the trust is critical.

ii. If your spouse is trustee, a general testamentary power of attorney will cause estate inclusion. So, care must be taken, and in such circumstances, you will want trustee powers to be limited by standards to prevent inclusion for certain types of trusts and certain trustees.

iii. The power of the trustee should include the power to invest property. California has the uniform prudent investor act, which under modern portfolio theory requires diversification, unless the trust instrument provides otherwise. If the trustmaker is heavily invested in a single class of assets (for example, real estate), this can cause a problem. In such circumstances, the trustee will have to liquidate assets, to diversify.

iv. Power over unproductive property – by granting the trustee power to retain or acquire unproductive or under productive property, this can prevent the forced sale of the family residence (even though it is not productive property).

v. The power to operate a business -- the trustee has the power to hold and operate any business or enterprise that is or becomes trust property. This is an important provision, as trust generally do not have the power to operate a business.

vi. Power to determine, for trust purposes, whether moneys are income or principle.

vii. The discretion to make distributions of income and principal, and the standard for distributions (i.e., 5 x5 powers or "health, education maintenance and support" (HEMS), which includes more than just medical bills and permits consideration of the beneficiary's standard of living, or a much broader "comfort, welfare, and happiness" standard).

viii. Payments for legally incapacitated persons, which permits the trustee to give the guardian (rather than the incapacitated person) payments.

i. Funding (Schedule A) -- A trust is <u>not</u> valid under law unless it has assets. It is therefore critical to identify the trust assets by listing them on a Schedule A to the trust. Applicable case law (<u>Estate of Heggstead</u> and <u>Estate of Ukkstead</u>) holds that a general assignment is acceptable (the attachment of a schedule of assets to the instrument and reference to it in the instrument) to qualify the scheduled assets as trust assets. Thereafter, if necessary, a <u>Heggstead</u> petition can be made to the Court for a <u>Heggstead</u> order permitting, i.e., the filing of a new deed, which generally can be obtained within sixty (60) days. The asset schedule must be up to date, with the schedule being one of the most important sections of the trust.

j. Funding with Additional Assets – a provision permitting additions to the trust is recommended for a revocable living trust (which is generally amendable), to permit the addition of assets to the trust. This permits flexibility, and is different from an irrevocable living trust, where the addition or subtraction of assets is not permitted.

k. Revocation and Amendment

i. Because at some point you may become incapacitated, it is recommended that you (i) grant a successor trustee the power to make distributions during your lifetime and (ii) articulate your rights to distributions in those circumstances.

ii. It is suggested that this be paired with designated powers under a power of attorney, to avoid the need for a conservatorship.

iii. It is also recommended that you allow the exercise of changes to the trust by third parties, in the event you are incapacitated. Correspondingly, among the powers given in the power of attorney, the agent should be authorized to amend the trust, for example, because of changes in the family and changes in tax laws. [Absent the power of attorney, a petition to the probate court for appointment of a conservator would be necessary, to permit changes in the trust in the event the trustmaker's disability. Under California law, if you put the provision in the trust, you also need to put it in the power of attorney document.]

l. Distributions – It is recommended that you give the trustee the power to defer distributions, to give the trustee a reasonable period of time to make distributions and not be forced to make distributions (for a 6-month to 9-month period). This will address circumstances when beneficiaries immediately start to spend money and therefore demand distributions.

m. Incapacity and Disability Planning – It is suggested that you have a provision providing that in the event of your in capacity, the agent under a power of attorney can demand distributions of income and principle. This will be particularly important if the agent is a different person than the trustee; and it can avoid the need to petition the court for appointment of the conservatory. The provision should also recognize the agent acting for you under a valid healthcare directive or comparable instrument.

n. Debts -- A provision directing the trustee to pay debts (including taxes) is recommended, to pay taxes, debts, expenses of administration, and the like. With that, distributions can be free and clear of debts, and you can prevent the possibility of creditors seeking to collect from your beneficiaries.

o. Account – The time period for objecting to account, if stated in bold language, can be reduced from three (3) years to 180 days, with everyone getting a prompt accounting. It is recommended that such language be stated, but that the right to an accounting not be waived.

8. Summary

We have reviewed the information you have provided, including your articulated goals. In light thereof, we recommend that foundational estate planning be put in place, including the naming of guardians for your minor children under a last will and testament. For the reasons described above, we recommend that you make a revocable living trust with a pour-over last will and testament. You can serve as trustee of your trust, but thought should be given as to whether you would like a co-trustee and who should serve as your executor under the pour-over last will and testament. Further, Art's sister is being considered as a successor trustee. That said, given the demands and potential length of the trusteeship, substantial consideration should be given as to who could serve in this capacity, and as a successor executor (if need be). In addition, a general durable power of attorney, healthcare proxy and living will, and HIPAA release are recommended, to plan in the event of your capacity and thereby avoid the need for a conservatorship proceeding. In making these documents, the above-described trust provisions should be considered.

We suggest use of A/B/C trust planning, using formula clauses to fund the bypass and marital trusts by use of a pecuniary bypass formula clause. Even if there is no estate tax concern, there are still reasons for creating a bypass trust. If the surviving spouse has creditor issues, you will want to lock-up the deceased spouse's assets, in case the survivor's assets are lost. If the survivor is in a high-risk profession, for asset protection purposes, you may want to lock-up the decedent's assets into a bypass trust. The risk of a later remarriage and a blended family is another reason, to make certain that your remainder beneficiaries (your children) ultimately inherit the trust assets.

The bypass trust planning might be paired with providing for a possible QTIP election for the marital trust. As stated above, this can guarantee that children inherit the trust assets, even if the surviving spouse remarries and later changes his or her plan. It can also be paired with an exhaustion clause, providing that the survivor cannot withdrawn any principal until his or her survivor's estate is exhausted. By planning this way, you provide a safety net for the surviving spouse but maximum protections that your children will ultimately inherit.

You will want to designate guardians in each of your Last Will and Testament, in the event something were to happen to you. As education savings is a goal, as you save and your assets increase you might consider establishing and your making contributions to Section 529 Plans. Your estate equalization concerns should be further discussed too.

To the extent Lynn is comfortable speaking with her parents regarding estate planning (particularly their current health), she might discuss with them gifts to Section 529 Plans (and their even frontloading with 5 years of gifting), and to the extent she might inherit a significant amount of money from her parents, given Lynn's asset protection concerns, her parents might consider leaving that in a third-party discretionary trust to protect trust assets from Lynn's creditors.

As indicated above, a complete Schedule A of your assets should be prepared. In doing so, all beneficiary designations should be considered and confirmed (retirement assets, life insurance, bank accounts, and more (as applicable), and all payable on death and transfer on death designations). All beneficiary designations with your assets should be checked and confirmed (or altered, as appropriate).

Given Lynn's liability concerns, it is recommended that your residence be owned as a tenancy-by-the entirety or by Art as his separate property. While the exemption amount remains high, you might also consider a transfer of your life insurance to an ILIT, with you retaining no incidence of ownership. Further, because your Roth IRA is regulated under ERISA, unlike your 401(k), for asset protection purposes rollover of a 401(k) into an IRA is not advisable. And your obtaining additional personal insurance (including an umbrella policy) should be considered. [And Lynn should obtain the maximum available and affordable professional liability insurance as is possible.]

Your articulated concerns with potential liability arising from Lynn's law practice should be addressed. A general partnership should be avoided, as each partner is liable for the acts of the other partner. Instead, a professional corporation, professional limited liability partnership, or a professional limited liability company is recommended.

To the extent any claims or potential claims exist, you must refrain from making any fraudulent transfer. Such a transfer can be reversed by a judge under the Uniform Fraudulent Conveyance Act (UFCA), can result in criminal penalties (California Penal Code §154), and could put Lynn's law license at jeopardy.

Finally, to the extent any contingency amount might be realized by Lynn and her law partnership and Lynn receives a significant inheritance from her parents, efforts to retain this as separate property (and any asset protection needs) should be discussed.