

Testamentary Trusts

Providing lifetime financial security for your family or other loved ones may be one of your most important estate planning goals. But how can you be certain that the assets you leave to your loved ones will be managed for their benefit — and according to your wishes — after your death? One way is through a *testamentary trust*, also called a *trust under will*.

A testamentary trust is an arrangement you create in your will. When you die, the trustee you've chosen manages the trust assets for the benefit of your family or other beneficiaries. Under the arrangement, your trustee is directed to distribute trust income and principal at the times and in the manner you have specified in the trust created under your will. Your trustee makes all administrative and asset management decisions, relieving your beneficiaries of this responsibility.

Planning with a Testamentary Trust

Testamentary trusts are very versatile and can play an important role in almost any estate plan. For example:

A testamentary trust can protect the interests of beneficiaries who are minors or simply inexperienced in financial matters, since the burden of decision making falls on your trustee. Knowing that your estate will be distributed exactly the way you have directed in your will can give you peace of mind in the present.

In addition to providing asset management, you can use a testamentary trust to make charitable bequests. Your trust can provide an individual beneficiary (or beneficiaries) with lifetime income and direct that the remaining gift property pass to the charity of your choice at the beneficiary's death.

You can use a testamentary trust to secure the estate-tax marital deduction for property that otherwise would not qualify for the deduction. You can set up your trust so that your estate may claim the marital deduction even though your surviving spouse receives only a lifetime income interest in the trust property.

You can also use a testamentary trust to unify your estate. By directing that employee plan benefits, insurance proceeds, and other similar payments be paid to your trust, you can ensure that all your assets will be managed together and distributed as you have indicated.

Common Types of Testamentary Trusts

There are several different kinds of testamentary trusts. Some common types are described below.

Life Insurance Trust. You create a life insurance trust so that the trust — and not you — owns your life insurance policies. This can be beneficial in reducing your gross estate — and potential estate taxes. At your death, the trustee collects the insurance proceeds, prudently invests them, and distributes them to your beneficiaries as you have specified in the trust provisions of your will.

Trust for Children. Should you and your spouse both die, a testamentary trust can hold your assets for your children until they reach a certain age. If your children are minors, such a trust avoids the need for a court to appoint a guardian or conservator for your children's inherited property.

Bypass (Family) or Credit Shelter Trust. You can use a bypass trust to minimize the tax bite on your surviving spouse's estate, leaving more for your children. Such a trust can maximize the use of both your and your spouse's federal unified credits, which allow up to \$5,120,000 in assets (per individual) to pass to heirs estate-tax free in 2012.*

* A 2010 tax law provision generally makes the estate-tax exclusion amount of a spouse who dies in 2011 or 2012 available for use by the surviving spouse's estate. However, a bypass trust strategy offers potential advantages compared to use of the portability election. Also, under current law, the portability provision is only temporary.

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Marital Trust. A well-constructed marital trust lets you provide lifetime support to your spouse without leaving your assets directly to him or her. Property in the marital trust qualifies for the estate-tax marital deduction. Marital trusts are often used with bypass trusts in an estate planning arrangement known as the *two-trust estate plan*.

Qualified Terminable Interest Property (QTIP) Trust. A QTIP trust is a type of marital trust that gives you complete control — through your trust agreement — over who will receive the trust property at your surviving spouse's death. With a QTIP trust, the executor or personal representative you've named to administer your estate may elect to use the unlimited marital deduction for the trust property, even though you give your spouse no more than a qualifying lifetime income interest in that property.

Other Benefits

A testamentary trust offers several other advantages for you and your beneficiaries, including:

Design flexibility. You can set up your trust with as much flexibility as you wish. You can give your trustee — or even a beneficiary — the discretionary power to use a certain amount of trust principal for an emergency, a child's or grandchild's education, or for any other reason you choose.

Longevity. A testamentary trust can be set up to benefit several generations of beneficiaries.

Future cost savings. Your testamentary trust may reduce future probate expenses and federal estate taxes that might otherwise be incurred by your beneficiaries' estates.

Professional asset management. If you wish, you can name someone with professional asset management and investment experience to act as trustee or co-trustee.

Choosing the Right Trustee

A trust is only as effective as the trustee you select to administer it. A well-qualified trustee is someone who has the knowledge and experience necessary to perform all the duties associated with managing and distributing trust assets — duties such as:

- Safeguarding the trust's investment assets
- Maintaining accurate records of all trust transactions
- Distributing trust income and principal according to the directions in your will
- Answering any questions your beneficiaries may have concerning the trust
- Handling day-to-day financial matters for beneficiaries
- Reporting to the probate court, when necessary
- Providing detailed statements of account and tax reports to the trust's beneficiaries
- Filing the trust's income-tax returns[®]

You may want to consider naming a professional to serve as trustee or co-trustee of your testamentary trust. A professional trustee provides continuity, unbiased judgment, and extensive investment and asset management experience and expertise, while relieving family members or other loved ones of the administrative burdens.

Does a testamentary trust have a place in your estate plan? A talk with your professional advisors can help you determine if a trust would benefit you and your family.

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