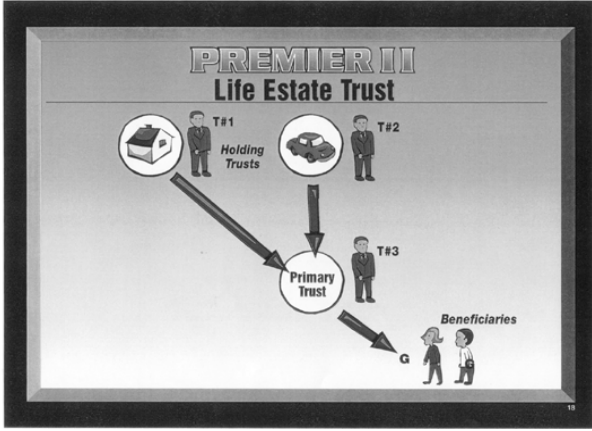

PREMIER PLAN II AND PREMIER Lite

LIFE ESTATE TRUST

SETUP AND OPERATING GUIDE ©



The National Association of Financial and Estate Planning

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CHAPTER 1. GENERAL INFORMATION

Note: This publication is designed to provide accurate and authoritative information in regard to the Premier II Life Estate Trust. It is provided with the understanding that NAFEP is not engaged in rendering legal or accounting advice. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.

Disclaimer. One of the important benefits of a Premier II Life Estate Trust is its ability to provide protection from lawsuits and liens. However, neither NAFEP, NAFEP Associates nor anyone else can guarantee that your Premier II Life Estate Trust will never be compromised by a legal action. No one can predict with certainty that you will set up and use your trust correctly or how a judge may rule in a given case. The best that we can be safe in saying is that, if you are sued, the use of your trust should allow you to fare significantly better than you would have without the trust.

INTRODUCTION

It is vital that the grantors, in conjunction with their professional advisors, read this guide to gain a better understanding of how the Premier Plan II Life Estate Trust should be set up and operated. There is a great deal to know about setup and operation, and this manual is the best source to get the information from. This manual was written to provide the trust grantors and their professional advisors most of the guidance that is necessary to gain the benefits that the grantors want from their trust.

Signing and notarizing the trust documents are important, but in order to obtain the benefits of the trust, it is absolutely imperative that the trust grantors transfer their assets into the trust (fund the trust). Only by funding the trust can the grantors' estate avoid probate, preserve the estate tax exemption of the first grantor to die, and receive all the other benefits that the trust can provide. See Chapter 3 of this guide for specifics on funding the trust.

PREMIER PLAN II LIFE ESTATE & PREMIER LitE TRUST

Premier II vs. Premier LitE. This trust program is available in two versions; the Premier II Life Estate Trust and the Premier LitE Trust. The main difference in these two versions is that the Premier II is a system, consisting of a Primary Trust and at least two Holding Trusts. The Premier LitE consists of a Primary Trust only (Primary and Holding Trusts will be explained later). The Premier II is intended for

families with many varied assets, specifically including a mix of real estate, vehicles and possibly business equipment. The Premier LitE is for simpler estates, usually with the personal residence as the only real estate, and having no vehicles or other dangerous property that will use or need trust protection or ownership. Throughout this manual we will use the term "Premier II" or "Premier II Life Estate Trust" to refer to both variations, unless we specifically note a difference.

Overview. This Plan is aimed at those American families that have small to medium sized estates. It is an ideal program for families whose estate we expect to be up to \$1,000,000 estate and gift tax exemption amounts (per person), as well as for families where estate tax planning will be taken care of by other means (such as NAFEP advanced gift and estate tax trust programs). This program is a direct competitor of and a plug-in replacement for a revocable living trust, though it is greatly superior to a living trust.

Advantages Over Living Trusts. The Premier Plan II Life Estate Trust is an irrevocable trust that delivers everything a revocable living trust does. Generally, living trusts offer:

1. Probate avoidance.
2. Prevention of outsider spouses from taking over estate property after the death of the first spouse,
3. Management and caretaking of the estate should the grantors become incapacitated and preservation of both estate tax exemptions of a grantor-married couple,
4. An exemption of up to \$1,000,000 of the first spouse to die (A-B provision in a living trust).

The Premier Plan II Life Estate Trust does all that, plus it provides the following:

Asset protection. Protecting one's property from creditors, lawsuits, divorces, Medicaid claims, liens and judgments.

Financial privacy. With this protection the Premier II can shield financial activities and property ownership from most private and bureaucratic snooping.

Limited liability. This feature means that the grantors (trust owners) can reduce or eliminate liability for damages, judgments and claims that may result from the ownership of certain types of lawsuit prone property.

Structure/Contents. The Premier Plan II Life Estate Trust functions much like the B portion of a revocable living trust, which is the portion of the living trust that is created upon the death of the first spouse. However, the Premier II Life Estate Trust is much more protective of your property than the B portion of the living trust. The Premier Plan II (excluding the LitE version) actually consists of three trusts, a Primary and two Holding Trusts. One of the Holding Trusts is intended to hold the family home, and the other is intended to own all family vehicles. The Primary Trust is used to hold financial assets such as bank, savings, and investment accounts. In addition, the Primary Trust is the controlling entity of the Holding Trusts. These three classes of assets - home, vehicles, and financial property - comprise the total estate of a large number of middle class Americans. Therefore, these three trusts will take care of the assets of most families. If the family has more property, or owns a business, other Holding Trusts and/or a business entity can be added. The grantors retain a life estate in all property, and are therefore the primary beneficiaries. They name their heirs as secondary beneficiaries, who take over the property after the grantors are deceased.

Trustee Arrangements. Each trust must have a different trustee, and the trustees must be independent of and not closely related to the grantors, or the trustees may be adult secondary beneficiaries (see next paragraph). The grantors may appoint a close relative, friend or advisor to the role of co-trustee. When a co-trustee is used, all major trust transactions require the signatures of both the independent trustee and the co-trustee. Since many grantors won't know three qualified, independent trustees, the simplest arrangement often is to use three NAFEP corporate trustees, possibly with one co-trustee serving alongside in all three trusts. The annual fee for usage of three NAFEP corporate trustees is typically very small, since the grantors will do most of the work involved in taking care of trust assets.

Grantors can pick any combination of their children (over legal age) to serve as trustees if the children are beneficiaries. If children are used as trustees there should still be a different one, or different group of them, over each trust. Use of children as trustees will compromise privacy, though, and that is always an important aspect of overall asset protection planning. Furthermore, the trustee who is a family member, may be subjected to family pressures and disputes plus a certain amount of liability. So the best choice often is for corporate trustees, with possibly an adult child (secondary beneficiary) as co-trustee. The trustee(s) can be fired by the grantors for a wide variety of reasons. Asset protection will remain in

place as long as the grantors replace the trustee(s) with another independent trustee or adult secondary beneficiary.

Asset Protection. Refer to the next chapter in this Guide, "Benefiting From Asset Protection", for details on this important aspect of a Premier II Trust.

Life Estate Provision. The Premier II Life Estate Trust is created with a hybrid, or enhanced, life estate provision. The grantors retain a life estate in all property placed in any of the three trusts. A life estate generally entitles the grantors to the income, use and benefit of their property. The Life Estate Trust adds these extra provisions:

- Greatly increased asset protection through the use of special trust provisions called "discretionary ", "fail safe" and "spendthrift" clauses.
- The grantors right to require any piece of property to be sold, and to direct the re-investment of the proceeds. For example, the grantors could require the sale of the family home, and the purchase of any other home, which may be smaller, larger, older, newer, etc.
- The right to change beneficiaries in any way (one time only) while both grantors are alive.
- Automatic inclusion as an equal beneficiary of any future children that come into the family.
- Optional provisions to divide trust property into halves, placing each half in a new and separate trust plan, in the eventuality of a divorce between the grantors.
- Prevention of a future spouse, after the death of the first spouse, from claiming an interest in trust property.
- An A-B trust provision that functions to preserve both estate tax exemptions when the grantors are a married couple (an exemption of up to 1,000,000 for each spouse).

Irrevocability. Irrevocability is a permanent protection for the grantors and their family. It is only a problem for outsiders, not the family. The Premier II Life Estate Trust can be revoked if the secondary beneficiaries (usually the children of the grantors) and the grantors provide a simple, written request or approval of it to the trustee. However, since the grantors have control and the benefit of the property at all times, there really isn't a reason to ever dissolve

the trust. The heirs will get whatever property distribution and usage the grantors decided on, just as with a revocable living trust. In fact, a life estate, irrevocable trust is essentially what a surviving spouse and heirs end up with in the "B" trust of an A-B living trust. Tens of thousands of A-B living trusts are created by estate planning attorneys every year, so the life estate "B" trust must be a good device. Except, why wait until one spouse dies to get asset protection, privacy, etc.? Why not start with a life estate trust to begin with?

Tax Status and Classification. All tax activities remain unchanged for the grantors. See the publication, which accompanies your trusts, entitled "Tax Return Preparation For (trust name)" for detailed tax information. Any trust income will be reported on the grantors' tax return. Any capital gains or depreciation will accrue to the grantors, to be reported on their personal return. The Life Estate Trust does not need a Federal Tax ID number unless income is earned by it. If income is earned in the trust, the trust must have an ID number and file a simple "zeroed" tax return each year. The trust pays no taxes since all income and gains are taxed on the grantors' personal return. The Federal Tax ID number does allow financial accounts to be set up under the trust's ID number instead of a grantor's social security number. This increases financial privacy for the grantors.

The grantors retain their capital gains exemption of \$250,000 per person or spouse on the sale of their primary residence. They may continue to deduct the mortgage interest they pay on their homes.

All of the gift and estate tax issues work exactly the same as they do with A-B revocable living trust. The Premier II is functionally the same device as a living trust for purposes of gift and estate tax planning. There are no gift taxes due as a result of transferring property to the trust. When the first grantor dies, his or her property interests are transferred to a "B" trust, if necessary, to preserve the decedent's gift and estate tax exemption of up to \$1,000,000. In most trusts the surviving spouse still gets to use this "B" share of the assets because his or her life estate interest is still in effect on all the property.

Grantor Controls, Miscellaneous Features. Grantors automatically are in complete control of the property's usage due to their life estate. Trustee signatures are required when property is sold, but the trustee has no option in executing the sale. The trustee's role is mostly a figurehead position during the grantors' lives. Grantors may release any part of their life estate interest at any time in the future in a simple procedure. This allows future estate tax

planning in estates that become too large for estate tax purposes. There is minimal paperwork during trust operation. Overall, trust setup and administration are very similar to that of a revocable living trust.

In a non-NAFEP life estate program, the grantors cannot consume the principal in the estate. They can only consume the interest or income, though they do have the use of the property. With the Premier II Life Estate Trust, the grantors can consume principal too. They may consume principal either by permission from the trustee, who can distribute principal to them for certain specific purposes, or by getting a simple written approval from the secondary beneficiaries (see the topic "Removing Trust Principal for Personal Consumption" in Chapter 2 for more information).

Accessories. Also included with the Premier II Life Estate Trust are the following, standard estate planning instruments: Pour Over Will, Durable Power Of Attorney, Medical Power Of Attorney, Advanced Medical Directive (formerly known as a living will), and Guardianship Appointments For Minor Children. Ask your NAFEP associate to explain the use and function of these important documents.

PRIMARY AND HOLDING TRUSTS

Primary Trust. The Premier LiE trust program consists of only a single trust, the Primary Trust, whereas a full Premier II also has Holding Trusts. The Primary Trust has three major functions. First, it is used to own and manage any of the family's financial accounts and paper assets. Second, it is the managing and controlling entity of the Holding Trusts. Third, it is the family estate-planning vehicle. All the family's estate planning provisions are contained in this trust. These functions make the Primary Trust the "master" trust, with the Holding Trusts being the "slaves."

The Grantors' financial assets, such as bank and investment accounts, corporate stock, life insurance policies, etc., should be held in the Primary Trust. It is not necessary or even desirable to create separate Holding trusts for financial or paper assets, since these assets are considered to be non-hazardous. That is, they will not generate a lawsuit. Hazardous assets, such as real estate, vehicles, equipment and business enterprises, should never be placed in this trust. Since the Primary is the beneficiary of the Holding Trusts, a lawsuit against the Primary Trust would be an attack on all the trust property.

Where the grantors operate a business enterprise or manage rental property, put the business or rental management activity in a legal entity such as a limited liability company. Do not allow the Primary

Trust to engage in any business activities that could lead to a lawsuit. For example, never allow the Primary Trust to collect or directly receive rental income from rental real estate. If there is ever a tenant lawsuit, the tenant will sue both the owner (a Holding Trust) and the landlord. Don't let the Primary Trust be the landlord. The same applies to any other business or business activity. Businesses are at too great a risk from lawsuits.

Important Note:

Therefore, keep hazardous, lawsuit prone property in appropriate Holding Trusts and financial and paper assets in the Primary. Do not conduct a business activity with the Primary Trust.

Holding Trusts. These trusts do three things. They either receive assets or dispose of assets. The trustees take directions from the trustee of the Primary Trust regarding when to receive or sell property. They may hold either personal or business assets. No day to day business activities are conducted with the Holding Trusts, they sit passively, holding legal title to their assets. These assets should all be physical, such as real estate, equipment, vehicles, etc. Do not open bank, financial or credit accounts, nor set up business locations or telephone numbers under these trust names. The idea is to keep these trusts as private, inactive and invisible as possible. The assets of any one Holding Trust cannot normally be affected by a lawsuit against any other trust, or a lawsuit against the trust grantors, the trustee or the beneficiaries.

If the grantors or beneficiaries want to sell property from a Holding Trust, the trustees of the Holding Trusts are required to take instructions from the Primary Trust and sign whatever documents are needed. When the grantors die, the Primary trustee will require the Holding trustees to sell any property that is necessary to fulfill the trust instructions regarding distributions to the heirs.

JOINT OWNERSHIP, COMMUNITY, AND SEPARATELY HELD PROPERTY

The information in this topic applies only to married couples and other two grantor trusts (such as parent and child), and does not apply to single grantors. Many couples have multiple forms of asset ownership. For example, a wife may individually own property she acquired before marriage, and the same may apply to the husband. In addition they may jointly own property which they acquired after their marriage. The individually owned property or assets are referred to as "separately held", and mutually

owned assets are referred to as "joint ownership". Ten of the 50 states in the U.S. treat joint ownership property between a husband and wife as "community property". The other states have different versions of joint ownership, such as "joint tenancy" and "tenants by the entirety". All 50 states allow another important form of joint ownership known as "tenants in common". (It is beyond the scope of this publication to explain these different forms of joint ownership.)

Most couples will want their assets to retain the same character of joint or individual ownership after the assets are placed into their trust. The wife may want to appoint her choice of beneficiaries for her separately held property, and the same for the husband. More importantly, they likely will want to retain control over their separately held assets after the death of their spouse or in the event of a divorce.

These concerns are provided for with a Premier II or Premier LitE Trust. Language in the trust specifically provides for the three possible ownership methods: Hers, his and joint. In community property states the trust provides for the community property form of joint ownership for jointly owned property within the trust. In other states the trust provides for the "tenants in common" form of joint ownership for jointly owned property within the trust. In all cases the trust allows for separately held property.

The different forms of ownership are supported by side documents which accompany a two-grantor trust. These documents are entitled "Schedule of Separately Held Property". There is one schedule for each grantor. The grantors individually fill out their respective schedule, listing their separately held assets. Then the two grantors cross-initial each schedule to acknowledge the separately held nature and correct owner of those assets. Each grantor will have their own control and beneficial interests separately held in their scheduled assets. All assets, which are not listed on one of these schedules, become joint ownership (50/50) in the trust.

DEATH OR INCAPACITATION OF FIRST GRANTOR

The Primary Trust contains various terms and provisions to handle an incapacitation of either or both grantors. For example, trust provisions require that assets be held and properly maintained by the surviving spouse and/or the trustee when one grantor becomes incapacitated. This is necessary to ensure that the incapacitated grantor still has his/her assets intact, should the grantor recover. It is also necessary in the event that there becomes a need of providing trust principal for the care or health of the incapacitated grantor. The family and trustee cannot

simply begin to distribute trust assets to beneficiaries, even when the trust has only one grantor, where that grantor is permanently or terminally incapacitated.

As a note of caution, when one of the two grantors dies or becomes incapacitated, there could be some ability of the surviving spouse to use trust property in a manner not allowed by trust provisions. This use might not be in accordance with the wishes of the dead or incapacitated spouse, if that spouse were able to speak or respond. It is important then for the beneficiaries to understand this potential liability, so that they can make sure the trustee is aware of the death or incapacitation of the first grantor. Both the beneficiaries and the trustee have legal recourse for any misuse or abuse of trust property by a surviving spouse. This does not mean that the surviving spouse can be prevented from full and normal usage of the property. It means that the surviving spouse cannot sell for personal gain or give away trust assets, or allow the property to become seriously or excessively degraded without trustee and/or beneficiary approval or involvement. It also means that no new spouse or companion of the surviving grantor can take control of any trust assets. The beneficiaries or the trustee can take measures to end or control any such activity by the surviving spouse. This feature is in the best interests of the deceased or incapacitated grantor, as well as the beneficiaries, and is what both grantors agreed upon when they ordered their trust.

BYPASS TRUST UPON FIRST DEATH

When a trust has a married couple as the grantors, most Premier II Trust instruments will provide for the creation of a "bypass trust" upon the first grantor's death. The bypass trust provisions call for the interests of the deceased grantor to be separated from the aggregated trust property and placed into the new, bypass trust. There are two reasons that a bypass trust is designed into a married couple trust. The first reason is to preserve the estate tax exemption of the first to die. The second reason is to identify and separately hold the decedent's interests, so that the decedent's heirs do not get cut out of the decedent's estate by inappropriate or neglectful use of the assets by the surviving spouse.

In larger estates, those that exceed the estate tax exemption of one person, failure to create and fund a bypass trust is an expensive mistake. If the decedent's interests are not physically segregated into an irrevocable bypass trust, the IRS will very likely treat those assets as being in the taxable estate of the second spouse to die. This means the estate

tax exemption of the first spouse to die is lost, and that will cost the final estate up to several hundred thousand dollars in completely unnecessary estate taxes. The only sure way to avoid this problem is to:

1. Physically create new trust documents with a different name for the bypass trust,
2. Obtain a separate Federal Tax ID number for the new trust,
3. Physically transfer property interests to the new trust name in a dollar amount that equals the value of the decedent's interests, and
4. Limit the surviving spouse's access to trust principal per the provisions of Federal Tax law. (The surviving spouse generally has the income; use and benefit of the bypass trust assets. In addition the surviving spouse can have as much trust principal as necessary, as long as the trustee is either a remainder beneficiary or an independent trustee.)

With married couples, each one wants to go their grave knowing that:

1. They have left the appropriate use of their share of the property interests to their surviving spouse, to use as he/she truly needs, but that,
2. The remainder will go to his/her children or heirs.

If the interests of the first to die are not physically identified and segregated, there is no way to assure, or even know whether those interests are appropriately used and preserved for the ultimate heirs.

Virtually all estate planners explain these provisions up-front to the grantors, and both grantors exception. Quite often, however, the surviving spouse forgets the wishes of the deceased spouse and opposes the formation of the bypass trust. However, the trustee is legally obligated to set up the bypass trust anyway, and could be sued by the beneficiaries for not doing so. The trustee is legally bound by the trust contract he/she signed with the decedent when the trust was created. The trustee is not bound by the illegal opposition of the surviving spouse. Even if the beneficiaries oppose the bypass trust creation, the trustee must still set it up. Otherwise, one of the opposing beneficiaries could later change his/her mind and then sue the trustee for failure to create the trust.

DEATH OR INCAPACITATION OF SECOND GRANTOR

When the second or only surviving grantor becomes incapacitated or dies, the trustee steps in and begins active administration of trust property, or makes arrangement with the beneficiaries to take care of it. There are specific provisions in the trust for the trustee and/or beneficiaries to take care of the needs of an incapacitated grantor, and any minor children there may be in the family. (There may be other heirs that need special care, too. The trustee will take care of them, financially, if that is called for in the trust. The grantors should make sure this provision for other heirs is in the trust if the need exists.) Once the second or only surviving grantor dies, the standard trust language calls for the trustee to divide the property equally among the heirs, sometimes distributed to them at different age milestones or over their remaining life times. However, your trust may provide for something different depending upon your specific needs.

IRREVOCABILITY AND AMENDABILITY

The trust is irrevocable, but amendable, in virtually any way, as long as the grantors, beneficiaries and the trustee all agree. In fact, the trustee is instructed by trust language to automatically amend the trust in any way necessary to conform to, or take advantage of new and applicable laws and court decisions. The trustee can amend the trust without permission in any way that benefits the trust, and that does not harm the interests of the grantors or beneficiaries.

When one grantor becomes incapacitated, or dies, that grantor's interest in the property is held irrevocably in the trust or in a bypass trust, and the trust cannot be amended in any way that changes the intent of that grantor. This is all necessary to protect the intent and wishes of the incapacitated or deceased grantor, since he can no longer speak for himself. The surviving grantor still has the above mentioned amendability over his/her own interests in the assets (usually a one half interest). The surviving grantor will in most trusts have the income, use and benefit of the property interests of the deceased grantor as well.

When the second grantor or only grantor dies or becomes incapacitated, that grantor's wishes and intents become locked in place by the trust. The beneficiaries who are identified in the trust can legally enforce this two step irrevocable process, and all the trust provisions, provided they have been made aware of their benefits and rights.

ESTATE PLANNING

The Premier II Life Estate Trust generally accomplishes the following:

1. Trust assets will be conveyed to the selected heirs or beneficiaries in the manner and timing the grantors have chosen.
2. Trust assets will avoid probate.
3. The trusts will prevent a surviving spouse from conveying assets of the decedent to a new marriage partner or to anyone else except the original designated beneficiaries (be certain to read the topic below, "Inform the Beneficiaries").
4. Trust assets may avoid twice as much in estate taxes for a married couple, than may be avoided with a non-trust estate.
5. The trustee can take care of trust assets if the grantors become incapacitated, in an orderly and legally controlled manner.
6. The trust usually has a provision that heirs receive their portion of the estate only after reaching a certain age. Often, the trust will specify that the heirs receive a percentage of their share at each of two or three different age milestones.

Most estate planning needs can be served with trusts, often better than with any other method of holding the assets. For example: Provisions for what happens if the grantors wish to provide for an heir who is disabled, if the grantors die with minor children, if the grantors want to make a charitable gift or want to change an heir's portion of the estate, or want to reserve some specific item or property for a certain beneficiary, etc., all can be handled with a trust. The Premier II application and order form, which the grantors filled out, was designed to disclose those concerns. But, if you as a grantor aren't sure, consult with the estate planner or NAFEP Associate who helped you for questions you now have. Some estate planning needs can be met after the grantors' property has gone into the trusts, but some can only be done before the property is put in.

There are some general provisions that your trust system probably contains that you should be aware of:

1. As long as all the original grantors are alive and legally capable, they have a one time, only, opportunity to change the beneficiaries of the trust in any way they want. (If the grantors retain the right to change the beneficiaries repeatedly, asset

protection will be seriously compromised, or totally lost). When one of the grantors dies or becomes mentally incapacitated, the beneficiary arrangement is locked in place for interests of the deceased grantor (usually one-half of the total trust), unless the beneficiaries themselves agree to further changes. This lock-in provision protects the wishes of the deceased grantor in regards to who will inherit and what they will inherit.

2. The trust will automatically include future children, whether by birth or by adoption, of the grantors as an equal beneficiary to the pre-existing children.

3. The trust can have an optional provision for dividing all property in half, and placing each half into separate trusts for each of the grantors should they decide to get divorced. Each of the new trusts would have the same beneficiaries that were named in the original trust system for each grantor's property interests.

4. If one grantor dies, the surviving spouse may re-marry and have future children with the outsider spouse. The trust usually has a provision that stipulates that such children will be entitled to an equal portion of the surviving spouse's half of the estate. This is because these future children are natural heirs of an equal portion of the surviving spouse's half interest in the whole estate.

INFORM THE BENEFICIARIES

While privacy and secrecy are important, it is vital that the beneficiaries be informed of at least some minimum details. If the heirs know nothing about the trust, which the grantors have, set up, they could lose some of what the grantors wanted them to have. One scenario that could cause a problem is when one of the two grantors dies, and the surviving spouse remarries someone who is not motivated to look after the best interests of the original beneficiaries. Other problems can occur when the grantors become elderly and fail to adequately take care of trust property or records. Another problem situation can arise when the grantors die or become incapacitated while possessing special knowledge that no one else is aware of, such as the details of certain projects or deals, the location of certain records, safe deposit boxes, etc. When a grantor dies, the surviving grantor could improperly collude with the trustee to take trust property to the harm of the beneficiaries. And, the surviving spouse will quite often strongly resist setting up the bypass trust. But that trust is necessary to protect the beneficiaries' interests. (See

the earlier topic "Bypass Trust Upon First Death" for more information.)

Beneficiaries can legally enforce their interests, and can be a significant factor in making sure the trust and trustee do what the grantors originally intended. As an extra measure of precaution, the grantors should consider the following recommendations:

1. Make the beneficiaries aware of the existence of the trusts, and the name, address and phone number of the trustee.

2. Make the beneficiaries aware of their rights and benefits.

3. Give the beneficiaries copies of at least the Primary Trust. It discloses their interests and identifies the Holding Trusts.

4. Inform the beneficiaries of the general workings of the trust structure (have them read or give them a copy of this guide) and fill them in on basic details, such as which trusts are the Primary, Holdings, etc., and what properties they contain.

5. Inform the beneficiaries of the location of all major trust, and other important, records. Make sure they can easily gain access to these records in any emergency.

6. Give a copy of all financial records, deeds, titles and conveyance documents to the trustee/trust officer and/or beneficiaries.

ANNUAL FEES

If you use a professional trustee either the grantors or the Primary Trust will be billed for annual trustee fees. For these fees the trustee does the following: Signs deeds, titles and special authorizations where required; analyzes these documents to see if they are proper; consults with, directs and advises the grantors on a wide variety of trust business; approves or disapproves of certain activities; may use trust funds to pay some of the important trust payments; keeps backup copies of important trust records; signs any trust tax returns (though no taxes are actually owed by a Premier II trust, the grantors pay all taxes); and is available on a moments notice to step in if the grantors are suddenly unable to take care of the assets. In addition, the trustee accepts financial liability for trust caused damages (in the rare case where the liability gets past the limited liability provisions of the trust). Normally, the grantors and beneficiaries have no liability at all for problems of this nature. The limited liability benefit alone is often

worth the price of the trustee fees. But, all the trustee's activities are critical in ensuring the integrity of this highly valuable financial asset, your trust(s).

TRUST DOCUMENT STORAGE

The grantors receive the original trust documents for safekeeping. The trustee/trust officer keeps a duplicate set of originals. But, other documents, such as deeds, bills of sale, titles, deposit slips, etc., may be generated by the grantors, and which are one of a kind. It is extremely helpful to give photocopies of financial records, deeds, titles, and other conveyance documents to the trustee/trust officer so that they can easily handle trust property in an emergency.

NAFEP recommends that the grantors place their original documents in a bank safety deposit box, or in a filing cabinet, lock box or safe that is fireproof, and that the trustee and beneficiaries all know about the location.

CHAPTER 2. BENEFITING FROM ASSET PROTECTION

Trust Asset Protection. Since all trusts in a Premier II are a type of irrevocable trust, and all (should) have independent trustees, each one is treated as an independent entity by the American legal system. Each trust is much like a corporation in its independent, legal status. This makes each one a separate owner, and the assets in each trust are owned by a different entity than the ownership of the assets in the other trusts. In other words, the family automobile has a different owner than the family home does, if they are in separate Holding Trusts. If something causes one trust to be sued, such as an auto accident in the automobile Holding Trust, the plaintiff has no cause of action or case against the other two trusts. The other two are independent of and unrelated to the automobile trust. In this example the plaintiffs could only get the automobile and any related insurance settlement. They could not reach the house or the financial assets.

If someone sued the grantor directly, any resulting judgment could not be applied to trust assets. The asset ownership is independent of the grantor. Going after the trusts, in this case, would be the equivalent of going after the grantors' neighbors because of a judgment against the grantors. Legally speaking, the grantors' heirs own the property in the trusts (though the Grantors have lifetime rights of usage and direct control of all assets). That is why the courts would not normally allow a claimant against the grantors to attach trust assets.

Another major factor in asset protection is the privacy involved. Once property is placed in a trust, it is titled in the trust's name. Routine snooping by outsiders will not reveal any property ownership by the grantors. It will be very expensive for outsiders to ever find out what the grantors do own (which legally is nothing!). The sheer cost and complexity of finding this out will discourage a large number of legal attacks from getting off the ground.

Beneficiary Asset Protection. In a discussion of asset protection for the parties of a trust, we must make a distinction between asset protection which is available for the grantors, and that which is available for the beneficiaries. Generally, asset protection is fairly absolute and straightforward when the grantors have died and the trust is providing some on-going benefits to beneficiaries. (Other mechanisms provide asset protection for the grantors though.) The trust's "spendthrift" and "discretionary" clauses take care of protecting trust assets from any creditors of or divorce actions against any beneficiary.

The spendthrift provision permits the trustee to use trust funds to directly pay the bills and expenses of the beneficiaries (after the death of the grantors, and for as long as the trust holds assets for a beneficiary). The beneficiary's bills and expenses can be handled this way, rather than by paying the money to the beneficiary. The trustee would only do this in the event there is a judgment against that beneficiary, and where the trustee felt the payment would be seized by the judgment holder. Rather than allow the payment to be confiscated, the trustee can pay the obligations of the beneficiary directly, bypassing the judgment. For example, the trustee could pay rent, utilities, loan payments, etc., directly to the creditors of the beneficiary, rather than make payments to the beneficiary.

These payments cannot be garnished by a creditor in all but one or two states. This small number of states do not allow spendthrift provisions to circumvent judgments and other legal obligations of the beneficiaries in this manner, so the trustee must check state law beforehand.

The trust may have a "discretionary clause" in place for the beneficiaries. When present, this clause says that the trustee has discretion over when, and how much, principal to pay out of the trust. The judicial system has uniformly protected the right of the trustee to use his "discretion" to withhold payments to a beneficiary when the payment is subject to creditor demands.

Grantor Asset Protection. Assets which are placed in the trust by the grantors must be protected from the grantors' creditors and judgments by other mechanisms. For example, in the case of the grantors the trustee's discretion to provide for the grantors must be limited. The trustee cannot have a requirement to provide for the general support of a grantor, even when that support is in the trustee's discretion, because payment of judgments and non-trust creditors can be considered part of the grantors' general support. So the trustee is generally limited to providing trust principal to the grantors only for short-term medical needs and for business needs. The Grantors' asset protection is accomplished by two features of a Premier II trust; the grantors' retained life estate interest and the "beneficiary termination" provisions.

The life estate interest, which is retained by the Grantors, limits them to the income; benefit and use of trust property. It does not allow them direct access to trust principal for personal consumption. Consider an example where the grantors have an investment account worth \$100,000 in the trust, and this account generates approximately 10,000 per year in income.

The grantors are automatically entitled to the 10,000 because that is part of what their life estate provides. The grantors do not need anyone's permission to take this money, it is theirs. But suppose now that the Grantor's want to take \$15,000 of the 100,000 principal and use it for an extended tour around the world. They cannot remove principal for such personal consumption. The principal belongs to the trust, for the eventual transfer to the beneficiaries. (There are ways in which the grantors can consume principal in this manner, which is discussed in the "Grantors' Use of Trust Principal" topic below.)

But the grantors cannot take direct control and charge of trust principal for purely non-trust, personal consumption. That is the essence and core of their asset protection. Since they cannot access the principal to pay for personal needs (which includes debts); their creditors cannot access the principal through them either. A creditor cannot force the grantors to pay with assets which the grantors have no ability to pay out. A creditor can only take from the grantors what they possess, and legally that is income only.

Important Note: Therefore, the most crucial concept and rule that the grantors must adhere to, in order to keep their asset protection in force, is this:

Never remove trust principal for personal use without going thru proper procedures. See the "Grantors' Us of Trust Principal" topic for more information.

Another powerful asset protection provision is the "Beneficiary Termination" clause, also known as a "fail safe provision". In this provision the term "beneficiary" includes the grantors along with the heirs who are the ultimate beneficiaries. This clause provides for a beneficiary's interests to be terminated if the interests are in immediate danger of being seized, liened or claimed, and where no other action can prevent this result. The termination cannot be carried out by the trustee unless there is no alternative to giving the assets, or control of them, to the grantors' creditor. In a worst case scenario, the grantors' interests in the trust would be terminated and their heirs, as the ultimate beneficiaries would take over the life estate.

It is very unlikely that this termination or fail safe provision would actually become necessary to implement. There is a legal principal that says a lien or seizure cannot be placed against a property that is not available for liening or seizing. Assuming that a

judge will follow this theory, no lien or seizure would be court ordered against Premier II assets, because that would trigger the beneficiary termination provision, and that makes the assets unavailable to lien.

Fraudulent Conveyance Considerations. All asset protection features of a Premier II trust are subject to laws against "fraudulent conveyance". The asset protection safeguards only apply to assets the incurred by the grantors. Once a damage, debt, or liability has occurred, even if no lawsuit has been filed, setting up the trust afterwards will not "legally" protect the grantors' assets from that specific liability. On the other hand each state does have a statute of limitations that prevents a litigant from suing after a few years. After a given time period, property in the trust is generally not subject to pre-existing problems.

Setting up a trust after a liability has occurred could be ruled as a fraudulent act by a judge hearing a lawsuit against the grantors. However, a finding of a fraudulent conveyance is a civil remedy, not a criminal issue. Fraudulent conveyances laws are primarily designed to give a litigant a remedy to place a claim on assets that were transferred by their owner after a liability occurred. Furthermore, fraudulent conveyances are usually very difficult and expensive for a litigant to prove. So even if a transfer is technically illegal, usually the grantors have everything to gain and nothing to lose by setting up asset protection with existing liabilities.

All Premier II trusts have a "Fraudulent Conveyance" provision, which basically states that it is not the intention of either the grantor or the trustee to have property in the trust which was fraudulently conveyed. The provision states that if a court having proper jurisdiction rules that a fraudulent conveyance has occurred the trustee will comply with any order regarding the property that the court issues. A conveyance can only be fraudulent if the property will not or cannot be made available following a court order, or the property's conveyance is intended to thwart a court order. The purpose of this language is to eliminate a fraudulent conveyance conviction by agreeing in advance to abide by any court decision, and to demonstrate that the grantors were acting in good faith when the trust was set up.

The subject of fraudulent conveyance is somewhat complex though, so be sure to consult with appropriate legal counsel if you have questions.

GRANTORS' USE OF TRUST PRINCIPAL

In order for the asset protection provisions of a Premier II Trust to work, the grantors must not have

the direct ability to consume trust principal for personal, as opposed to trust purposes. In almost all cases this is no problem because the grantors will not often need to spend trust funds on something that is not trust business. For example, suppose the grantors want to replace the roof on the family home. If the home is in the trust, which it certainly should be, it is not personal consumption for the grantors to liquidate part of the trust investment account so that the roof can be replaced. This is merely a conversion from one type of asset (cash) into another (real estate). No value has been lost or removed from the trust. The same idea would apply if the grantors wanted to purchase an additional vehicle with trust assets. As long as they put the new vehicle in the trust, they are not removing principal or value, merely converting it to another asset type.

This concept also applies to the sale of trust assets. If the grantors wish to sell the family home and purchase another, even if the new one is either more or less expensive, there is no problem as long as the value remains in the trust. When the old home is sold, any cash proceeds after paying off the mortgage will need to go into the trust. When the new home is purchased, it must go in the trust. The final result will be a zero change in trust net worth. No principal has been removed by the grantors and the grantors' goals have been accomplished.

If the grantors think they may need significant personal consumption of their principal, maybe they should not put all their assets in the Premier II. For example, assume that the grantors are retired and cannot live on their pension and investment income alone. They will need to cash in some of their savings from time to time for ordinary living. In that case, that amount of savings should be left out of the trust. If the grantors want asset protection for the savings they should consider purchasing a commercial annuity with the savings, because annuities are afforded their own creditor protection in most states.

Removing Trust Principal for Personal Consumption. If in spite of the best planning the grantors find that they must remove some trust principal for personal use, they must use the following provisions to keep their asset protection in force:

1. The trustee is allowed under trust provisions to provide principal to the grantors for limited purposes. These purposes include short-term medical care and needs (as opposed to long term or institutionalized care), and the business needs of the grantor. If, for example, a grantor needs cash for startup or working capital in his/her business, the trustee can dip into trust principal

for that. Any short term medical needs of the grantors can be provided for as needed by trust principal. Under this provision the trustee should either personally write and sign the check transferring the principal sum to the grantors, or should write a memo to keep with trust records giving approval of the decision to provide the principal and its intended purpose.

2. The trustee is allowed to lend trust funds for any creditworthy purpose. The trustee can make small, non-collateralized loans to the grantors, but larger amounts (in excess of 5% of trust net worth) should be secured. To establish the loans as real, there should be a formal note signed by the grantors, bearing a rate of interest in line with the current market, and a provision of collateral by the grantors on larger loans they take out. The note should have a definite repayment provision and the grantors should meet the repayment schedule.

3. Any adult beneficiary (remainder beneficiary) who has at least a 5% remainder interest stated for him/her in the trust, can give permission to the grantors to use trust principal for any reason, at any time, for any amount. As long as the grantors have at least one child or other trust heir whom they can work with they should have no problem obtaining the needed permission to take principal. If this is ever done, it should be documented by a simple written statement of permission, signed by the beneficiary. This written statement must be kept with trust records by the trustee and grantors.

PROTECTION FROM LEGAL DIFFICULTIES

Whether the trusts become subject to a judgment, or fail to deliver any benefit that the grantors expect, will depend largely on trust setup and operation. It will not depend as much on the wording in the legal documents themselves. In a legal dispute the courts and bureaucrats will always look beyond the legal language of the trust and into its actual operations. The grantors, with the assistance of the trustee or trust officer, are in control of and responsible for the integrity of the trust program. They must personally ensure that setup and operations are handled generally in line with this "Setup and Operating Guide".

By trust "setup", we are referring to a couple of items. The first is the fact that the trust cannot be used to avoid payment of existing creditors. If the grantors have unsettled tax assessments, liens or judgments of any kind, pending or potential liabilities from some past activity, or any other debts,

arrangements must be made to take care of these either before or after property goes into trust. Placing property into trust to avoid paying a debt or a potential debt is a fraudulent transfer, even if no litigation has yet occurred. (See the above "Fraudulent Conveyance" topic for more information.)

The second thing we mean by proper trust setup, is the correct conveyance of property into the correct trust, and the correct setup of any bank or financial accounts. Naturally no trust benefits can be achieved until the grantors' property is correctly under trust ownership. Doing it correctly means following the verbal instructions from your estate planner or appropriate professional advisor, trust officer or trustee, and the instructions and guidelines of this manual.

By trust "operation" we mean doing the routine details which occur when the trust is a real and independent legal entity, and not a sham substitute for the grantors. This means that the trustee must be independent of the grantors (not closely related by blood, marriage or employment), or the trustee must be an adult beneficiary, and the trustee must be the owner of the legal title to all property in the trust. Merely having the trust documents state that there is a trustee separate from the grantors is not enough. If the grantors routinely handle everything just as they did before the trust existed, if they co-mingle personal business with trust business, if they consume trust principal without permission, then the trust may not be a valid asset protection entity.

Proper operation also means the trustee should be the primary signer on trust bank or financial accounts where there are significant amounts to be held in the accounts. The grantors should receive only income, not the principal, from those accounts for maximum asset protection. If the grantors take any of the principal from a financial account or take any asset without trustee and/or beneficiary approval, then a successful lawsuit against the grantors can force the trustee to turn over the rest of the principal to the judgment holder. The trustee or trust officer should actually write and/or sign the checks for principal distributions to the grantors. Distributing trust principal to the grantors should not be a routine occurrence without the secondary beneficiaries signing off for it. It is best if the grantors maintain their personal bank account outside the trust so that there is no chance of a creditor or court assuming the use of that account is an indication of the grantors' control over the trust.

Deeds and titles must place property in the name of both the trust and the trustee when property is put into the trust (see Chapter 3 for details.) Deeds and

titles must be signed by the trustee whenever property is sold. The grantors should never insert their name on any trust-related document where an owner's name is required. The trustee's name should be used in those cases. The trustee/trust officer should approve and supervise borrowing and/or lending of any substantial sums or assets of trust property. Any chance to involve the trustee/trust officer in trust affairs in writing, on a fairly routine basis, should be taken.

If the grantors and trustee fail to follow these concepts and requirements, and/or fail to keep the written records of it, they are playing Russian roulette with the independence and the asset protection of the trust. In many cases the grantors can overstep their authority without the trustee being aware of it. Therefore, it is vital that the grantors act carefully and give serious attention to bringing the trustee in on any unusual, legal, or other important issue.

Privacy and Secrecy. One of the primary advantages of a Premier II is the privacy that can be maintained with trust assets. This privacy and secrecy is one of the key barriers to invasion. Therefore, guard this protection closely. Do not disclose to acquaintances, relatives (other than the grantors and beneficiaries), associates at work, bankers, financial advisors, attorneys or accountants/tax preparers, any trust details that could compromise privacy and security, unless there is a good business or financial reason to disclose something to them. Even though these individuals may be professionals, or supposedly reliable confidants, they may have hidden agendas and/or legal obligations that you are unaware of. They may be just plain gabby. Also, they may get subpoenaed to testify in court or in a deposition as to what they heard you say. Purely casual conversation has led others into lawsuits or turned into legal testimony in many lawsuits. So keep your affairs as private as your dealings will allow.

A further measure of trust privacy can be added by using a Post Office Box or a separate business location for the official address of each trust. It is preferable to have the trust address be different from the grantors' home address. This can be taken one big step further by having your trust domiciled in Nevada (see next topic).

When real estate is conveyed to a trust, the deed becomes a part of public records. Unfortunately, the deed will show the name of the former owner of the property, which is the grantor of the trust. This is not necessarily a problem, but you may desire more privacy than that. To keep your names off the deed, consider deeding the property to the Primary Trust,

first. Then, deed the property from the Primary to the appropriate Holding Trust. Most outsiders when researching ownership of a piece of property would look only at the most recent deed. That deed would show the Primary Trust as the old owner of the property and the Holding Trust as the new owner (neither trust should have your family name as part of its name). When your names are not found on the deed the outsider will likely conclude that you have nothing to do with the property. Both deeds can be prepared at the same time and recorded in one trip to the County Recorder, but the second deed should be dated at least one day later than the first. This strategy will cost a few dollars more, but it can contribute substantially to privacy and to the protection of real estate from legal difficulties.

NOTE: Do not include life estate language on a deed! Life estate language on the deed overrides and restricts the life estate provisions of the Premier II and reduces the grantors' privacy.

Nevada Domiciling. One of the most significant added steps the grantors can take to make a Premier II more bullet proof from lawsuits is to domicile their trusts in the state of Nevada. The term domicile as used in this context means: The state having legal jurisdiction over the trust, and the state of physical residence of the trust. To make this effective, all the trusts, both Primary and Holding, must be Nevada domiciled.

NAFEP can provide Nevada domiciling for your trust program, either through a NAFEP Associate, or you may contact NAFEP directly for this service. The cost for this Nevada domicile program is very nominal. Nevada domiciling provides the following services for a Premier II trust:

1. A Nevada physical and legal domicile,
2. A Nevada physical and PO Box mailing address,
3. A Nevada phone number,
4. Accessibility to Nevada based banks with nationwide bank branches for opening trust bank accounts,
5. Nevada mail and phone call messages forwarded to the senior trust officer, or to the Grantors, whichever is appropriate and/or agreed upon.

Note: These services by themselves do not include trustee/trust officer fees.

When Nevada domiciling is used correctly and fully, all trust mail and phone calls will be directed to the Nevada location. All financial accounts, annuities, life insurance policies, property deeds recorded in the trust, etc. will be set up with or changed to the Nevada address. All real estate tax notices will go to Nevada. If a trust bank account is opened, it will be done at a Nevada bank or bank branch. Further, a Nevada based and domiciled trustee must be used. These actions, especially the Nevada trustee arrangement, place the legal ownership of trust assets physically and legally in the State of Nevada. In the case of financial assets, they may only be attacked by a creditor or plaintiff in the State of Nevada because those assets will have no physical or legal presence in any other state. Real estate, of course, will be located in the state where the grantors acquired it, so a creditor can attack that trust property in that state. But the legal ownership is still in Nevada.

The value of Nevada domiciling is as follows:

1. The trusts will be governed under Nevada laws, which are among the most pro-grantor, anti-creditor trust laws in the U.S. (For example, even "self-settled, spendthrift trusts" have creditor protection for the grantors in Nevada, one of only a small number of states to offer that benefit to trust grantors.)
2. If a creditor succeeds in getting a judgment directly against the grantors, the creditor would in all likelihood be forced to have court hearings regarding lien or seizing trust property based on Nevada law. This is the case regardless of the state that the Grantors were sued in. If a lawsuit is initiated against the grantors outside of Nevada, the non-Nevada court should be bound to use Nevada law in making decisions. As stated above, Nevada laws are unfavorable towards creditors and judgment holders when it comes to taking appropriately titled assets from an irrevocable trust.
3. If a creditor succeeds in getting a non-Nevada court to grant a lien or seizure action against a Nevada domiciled trust, the creditor must (if the courts act as expected) then go to a Nevada court to get the action enforced in the state of Nevada. Remember that with Nevada domiciling the property is owned by a Nevada trustee. In a worst case scenario, the non-Nevada court could allow lien or seizure of *real* and *personal* property which is physically located in the non-Nevada state the court is in. But the non-Nevada court has no jurisdiction over and cannot grant those actions* against the *financial* assets when those

assets have been properly titled in Nevada. With proper Nevada domiciling, financial assets will be physically held and owned by a Nevada trustee inside the state of Nevada.

* In a worst case scenario, the non-Nevada court could hold the grantors in contempt if they refused or were unable to have assets returned from Nevada to satisfy a judgment. This result is very unlikely, in the opinion of NAFEP legal counsel, due to fact that the Grantors have no means of complying with the order, and contempt of court rulings must be used only for coercive, not punitive, reasons in civil cases.

4. Before the creditor ever gets to a Nevada court for enforcement, the trust can be re-domiciled in still another political jurisdiction. The creditor would be unaware that re-domiciling was taking place until he had expended tremendous time and money. In a worst case scenario, that of a judgment against the grantors and an enforcement action of the judgment against a Premier II Trust, this re-domiciling makes it unlikely that the creditor would obtain trust assets.

ASSET PROTECTION FOR PENSION PLANS

No government regulated (IRS qualified) pension plan may be transferred to a family trust. There may be some private and non-IRS qualified plans that can. In those cases, consult with a plan representative on what to do with that type pension. But the IRS qualified plans, such as 401(k), IRA, Keough, Defined Benefit, etc. are already a trust, defined and regulated by federal tax law. These qualified plans cannot be held by another trust, such as a Premier II.

One group of pension plans, known by the name "ERISA", is asset protected from general creditor claims by federal tax law. IRA plans, which are not an ERISA type, have no *federal* protection from creditor claims but many states protect these plans from legal actions under state law. Check with a NAFEP Associate or consult a local attorney to find out about your state's protections for IRAs. However, these federal and state asset protection laws generally do not prevent spousal, child support or unpaid tax claims from attaching to the pension plan.

LAWSUITS & OTHER LEGAL MATTERS

Whenever any significant legal problem arises, remember two rules:

- Initially, don't sign, negotiate or communicate anything to the adversary party, and
- Contact your trustee/trust officer or NAFEP immediately. In some cases a correct response must be given in ten days or less.

If your trustee/trust officer is a professional or a NAFEP Associate, he or she has a wealth of information available to help with legal problems and may be able to handle the problem directly. Professionals can also provide much specific information to the trust or grantors' attorney to use if attorneys are required in dealing with the problem. NAFEP will not contribute financially to the legal costs of defending a trust, but NAFEP is one of the best information and consulting resources for the attorneys who are handling the defense. But, among the advantages of this trust program are that many problems can be taken care of without hiring expensive, outside advisors, and most problems will go away or be settled without litigation because of the privacy and difficulty of penetrating a Premier II Trust.

CHAPTER 3. FUNDING AND SETTING UP THE TRUST

The process of funding (transferring assets to) a trust faces some time constraint concerns. It is important that all assets be conveyed into the trust in as short a time frame as possible. This is necessary to help avoid the problem of encountering a lawsuit, grantor illness or death in the middle of the setup process. In addition, the trust is worthless or not fully effective without the conveyance of all intended property into it.

RECORD ORGANIZING SYSTEM

Each trust of a Premier II has its own tabbed divider section in a deluxe binder. Each trust is placed in a double-sided pocket file folder in that trust's section. This folder allows each trust to be kept in the front pocket of its folder, with the pertinent records of that trust being kept in the back pocket of the same folder. The Primary Trust documents should contain a listing or should physically hold records and the actual documents of all financial accounts, insurance policies, bills of sale, stock certificates, etc. which name the Primary trust as owner or beneficiary. Each Holding trust should have its applicable real estate deeds, vehicle titles or bills of sale, which pertain to that trust. If the records and documents are not kept with the applicable trust, there should be a statement with each trust indicating where its records may be found. Proper record storage and availability are vital when the heirs and trustee need to step in and take care of trust business.

BANK ACCOUNTS

Opening New Bank Accounts. The trust does not need a bank account unless the trust receives income, especially from multiple sources. In many cases, trust investments will be held in a brokerage account which has check writing privileges, making a separate bank account unnecessary. (The grantors should never use a trust bank account, which holds trust funds, for personal business. That negates another reason to have a trust bank account.) So, most Premier II trusts will not require a bank account. If one must be opened, use the following procedure: Take a copy of the "Certificate/Affidavit of Trust" plus the "Trust Resolution and Banking Authorization" to the chosen bank. Both these documents are furnished with the trust. Do not furnish your bank with or allow them to make a photocopy of your entire trust. This compromises privacy; they do not need this document and cannot legally require it.

Request from the bank a trust account. Most banks are unaccustomed to opening trust accounts except for revocable living trusts (where the grantors are trustee, grantor and beneficiary). This trust is different and often causes some confusion for the bank employees. The main thing to get across to them is that this trust is an independent legal entity (like a corporation). If the bank cannot make the Premier II conform to their type trust account they may want to open a general business or commercial account instead. This type account will work for the trust too.

The name of the account and the name printed on the checks should be the name of the trust. Do not allow the names of the grantors to be used on the account or on the printed checks as account owners. The bank will require a Federal Tax ID number to open the account. This number will be furnished with the trust (and listed on the "Trust Resolution") if a Tax ID number was requested on the NAFEP trust application and order form. Do not allow the bank to use the personal Social Security number of the grantors, trustee, or beneficiaries as the identifying account tax number. That can confuse account ownership, which can result in serious problems later. Require the bank to use the Trust's Tax ID number as the tax number of the account. The bank may want to list the account signers' Social Security number for identification purposes only and that is acceptable.

The trustee should be the main or the only signer on the account. It is acceptable to have a co-trustee appointed who acts as a required co-signer, and the grantors may be signers on the account as well. None of the co-trustee or co-signing arrangements will compromise the asset protection of the trust unless the grantors violate the limitations on taking trust principal, or unless they use the account for personal and non-trust business. If the grantors can independently sign checks, without the trustee co-signing, they may take trust income freely, because that belongs to them automatically.

If grantors or beneficiaries are account signers, they can act as "managers" of the account, and use their address as the account address. This allows the bank statements and blank checks to be mailed to that address. In that case, the main trust documents should contain information indicating where the bank account is held, and where the account records and checks are kept. This will help the trustee to step in and take care of trust business when that becomes necessary. This "management" role must be defined in writing, so a "Caretaker/Management Agreement" is provided with the Primary Trust.

None of the foregoing information about signing on a dedicated trust account will prevent the grantors from opening a personal account under the trust name, as long as the account does not contain trust funds. If the grantors do this, they can use the account in any way they want; though there will be no asset protection for the account. The only reason to open a personal trust account is to gain additional financial privacy for the grantors' bank activities.

Existing Bank Accounts. The grantors may have existing bank accounts or brokerage accounts with check writing privileges, which they use primarily for personal business. These accounts should not be placed in the trust. If the account balances are so large that there is an asset protection concern, then remove some of that balance and put that amount into the trust. But don't put the personal business account itself in the trust. It is important not to commingle trust and personal business.

However, the grantors do want the account balance to go to the trust upon their deaths. Therefore go to the bank or financial institution and ask for a "payee on death" (POD) provision for the account. Then list the Primary Trust as the POD. This provision specifies that upon the death of the last account owner/signer, the remaining balance is to be paid to the trust. In other words, the trust is the remainder beneficiary of the bank account. This allows the grantors to use the account without hindrance during their life, but assures that the balance will go to their heirs according to the plan in the trust.

FINANCIAL AND BROKERAGE ACCOUNTS

The Primary Trust is furnished with a form letter that may be used to change ownership to the trust for financial accounts and brokerage accounts. (This topic is not referring to bank accounts. For information on that, see the topic above.) This letter can be identified by the greeting line, which says, "To Whom It May Concern" (see a sample at the end of this publication). The blank form of this letter should be copied, making a copy for each institution which is to receive one. After filling out the blanks in the letter, each grantor or spouse signs the letter in front of a notary. The final step is to send the notarized letter to the appropriate institutions. In many cases, these institutions will simply send back their own special forms for completion and signing, so the form letter we are discussing here has limits to its usefulness, and in fact its usage is optional. The letter can, however, be used as the initial communication to these institutions, which prompts them to send you their forms.

Filling out and signing these letters can be legally binding transfers. The letters may therefore be useful in requiring the institutions to complete the ownership changes even if the grantors die or become incapacitated before the accounts are changed. Further, these letters are a good way to fully identify up front all the grantors' financial accounts and instruments that need to be in the trust. Execution of these letters right away is a good idea for these two reasons alone.

ANNUITIES

Normally, you will want to make the Premier II or Premier LitE Trust the primary beneficiary and owner of commercial annuities. This is due to the need to provide trust management for the large, lump sum payoffs in the event of the annuitant's untimely death. However, it is vital that the insurance company which is the annuity issuer understand the nature of the trust ownership of the annuity. Otherwise there may be negative tax consequences.

The Premier II and LitE Trusts are legal owners of annuity contracts, and are legally entitled to have tax deferred status in annuities because of two facts:

1. Both trusts types are a "grantor" trust under Internal Revenue Code (IRC) Sections 671-678,
2. Both trust types are an agent for a natural person under IRC 72(u)(1).

If the insurance company fails to know and to fully comprehend these two facts, they will:

- ✓ Treat transfers of existing annuities to the trust as a taxable event, and issue a 1099 to the annuitant.
- ✓ Treat the purchase of new annuities by the trust as not having tax deferred status, and issue annual 1099s for the income of the annuity.

To assist with the transfer of existing annuities to the trust, NAFEP supplies a special transfer letter for annuities which is included with the other transfer documents of your trust. This letter can be identified by the line, near the top, which says, "Re: Change of Owner and Beneficiary of Annuity Contract(s)". This letter has the above mentioned tax law citations and hopefully will work with your insurance company.

However, some insurance companies are uncooperative in either the transfer to or the issuance of annuities to trusts. They may refuse to assist you

at all, may state that a 1099 will be issued upon transferring ownership to the trust, or they may state that no deferral can be had with a new purchase. If you encounter these problems, existing annuities can be transferred from uncooperative companies to a company which is cooperative through the use of a procedure known as a "1035 exchange". For new annuities, simply shop for an insurance company which is cooperative. Rely on your NAFEP Associate or licensed securities rep for assistance in this area.

LIFE INSURANCE

Normally, the grantors will want to make the Primary Trust the primary beneficiary and owner of life insurance policies. This is due to the need to provide trust management for the large, lump sum payoffs and the importance of protecting cash values and death benefits from creditors. In addition, the surviving spouse's primary needs will often be met with retirement income and existing property of the grantors. If the surviving spouse needs income from the insurance benefits, the trustee can provide those needs without any problems.

The best way to make changes in life insurance ownership and beneficiary arrangements is to contact either the agent who sold the policy, or contact customer service at the life insurance company. There is an "absolute assignment" letter included with the trust which can be filled out and sent to the agent or to the insurance company as a way to initiate contact, and as a way to document up front what policies are to go into the trust.

Note: Be aware that by intentional design a Premier II trust does not remove any value from the grantors' taxable estate. As a result the death benefit of life insurance policies in the trust will be included in the taxable estate of the insured, or the surviving spouse. If the death benefit is large enough to cause an estate tax problem the grantors should seriously consider putting life insurance policies in an irrevocable life insurance trust, such as NAFEP's Premier V Irrevocable Life Insurance Trust. See a NAFEP Associate for more information.

EMPLOYER BENEFITS

Usually, the employer is the owner of the life and disability plans that it furnishes its employees. But consider making the trust either the beneficiary or the contingent beneficiary of the benefits plan where applicable.

RETIREMENT AND BENEFITS PLANS

NAFEP includes in all Premier II Life Estate Trusts special pension planning language. The special pension section of these trusts (entitled, *Trust as Beneficiary of Pension Plans*) gives the trustee all the power and flexibility necessary to deal with qualified plans in order to minimize income and estate taxes, and allows for IRA stretch planning. The pension section includes the necessary language to satisfy IRS requirements.

Where the trust is to be the beneficiary of a pension plan, the special pension section provides: (a) That the trust is or must become irrevocable upon the death of the grantor and pension plan owner, (b) the trustee is empowered to make up any deficits below the minimum distribution requirements of the pension plan (otherwise, the deficit would be taxed at trust rates, rather than the beneficiary's rate), (c) special provisions to qualify the trust as a "designated plan beneficiary", (d) that the beneficiaries must be individuals who are identifiable from the trust document, and that the trust can not leave plan benefits to a class of beneficiaries or a charity, and (e) the trust document must be provided to the plan custodian or administrator.

This means that a NAFEP family trust document is a legally proper and sufficient vessel for planners to use when implementing pension transfer strategies. When should a trust be named as the beneficiary of an IRA or other pension plan? Very generally, here are some guidelines:

1. Where the pension plan is large, presents an estate tax problem, and the plan owner is married, then: Consider naming a NAFEP Premier I or II family trust as the primary beneficiary of the plan. For married couples, the trust allows the trustee to make the surviving spouse a life beneficiary of the plan. This causes inclusion of the plan in that spouse's estate, while at the same time preserves stretch distribution provisions for remainder beneficiaries. Including the plan in the surviving spouse's estate, via the unlimited marital deduction, gets the plan out of the deceased owner's estate and gives the surviving spouse a chance to spend the plan down to a manageable estate tax level. Other assets can then be placed in the deceased plan owner's bypass trust to benefit from the decedent's estate tax exemption for those assets. In any case, the trustee will do the planning and make appropriate decisions after the death of the plan owner, and the trust gives the trustee both the power and the flexibility to do

whatever provides the best tax and estate planning result.

2. Where a married plan owner's pension assets are not likely to cause an estate tax problem, and especially where the surviving spouse is likely to use up most of the plan, it will often make the most sense to name the plan owner's spouse as the primary beneficiary, rather than the trust, and then name the trust as contingent beneficiary in case the plan owner survives his/her spouse.

3. Where a plan owner is not married, there are multiple beneficiaries among whom the plan is to be divided, and regardless of whether or not the plan is likely to represent an estate tax problem: The trust should be named as primary beneficiary. Of course there can be no estate tax planning via the marital deduction with an unmarried trust grantor, but the trust does provide for stretch planning, to minimize income taxes, among the remainder beneficiaries.

4. Where a plan owner is unmarried, there is only one heir who will be beneficiary for the plan, and regardless of whether the plan is likely to cause an estate tax problem: It may make sense to name the one heir as direct primary beneficiary of the pension plan, and name the trust as a contingent beneficiary. But, if the primary beneficiary is a minor, it may be best to name the trust as the primary beneficiary of the pension plan, with no contingent.

Basic IRA Stretch Planning Concepts:

Note: The Following is a reprint of an article in the December, 2003 issue of *Estate Planning* journal, written by The Estate Planning and Administration Group of Schiff, Hardin & Waite, a large law firm and pension planning expert resource located at 6600 Sears Tower, Chicago, IL 60606-6473, e-mail: estateplanning@schiffhardin.com."

"Trusts as beneficiaries of retirement benefits continue to cause problems for estate planners, in part because of unnecessary complexities foisted upon us by the IRS. Final Regulations issued by the IRS permit a trust to be a designated beneficiary if certain requirements are met. They include that the trust must be valid under state law, the trust must be irrevocable no later than the death of the account owner, the beneficiaries must be identifiable, and certain documentation must be furnished to the plan administrator or IRA custodian by October 31 of the year following the account owner's death."

"If all these requirements are met, and assuming that only individuals can benefit from the retirement plan or IRA proceeds, then the oldest beneficiary of the trust is deemed the "designated beneficiary". It is this designated beneficiary whose life expectancy can be used to determine the minimum distributions required from the plan or IRA. If there is no designated beneficiary, the remaining proceeds have to be paid out over a five-year period (if death occurs before the required beginning date) or over the projected remaining life expectancy of the decedent immediately prior to death (if death occurs after the required beginning date)."

"In some situations, using the oldest beneficiary's life expectancy is not a significant hardship. If the ages of the client's heirs are only a few years apart, the difference in the minimum distribution requirements from oldest to youngest is probably relatively small. On the other hand, if the range of ages of the heirs is greater, as may be the case if the client has children from different marriages, there can be a significant loss of benefits to the client's family if the oldest beneficiary's life expectancy must be used for all the beneficiaries."

"Under IRS Proposed Regulations, it appeared that as long as subtrusts for the children were created immediately at the account owner's death, the "separate account rules" would permit each child to use his or her life expectancy for purposes of distributions to his or her trust. However, the final Regulations eliminated that provision and instead say that the separate account rules "are not available to beneficiaries of a trust with respect to the trust's interest in the employee's benefit." (Reg. 1,401(a)(9)-4, Q&A-5(c).) Three related private letter rulings confirm that the IRS no longer believes that the separate account rules apply in this case."

"In IRS Letter Rulings 200317041, 200317043, and 200317044, the decedent died at age 60 with an IRA. The decedent had designated his revocable trust as his beneficiary, but had also provided in the beneficiary designation that the trust was to be divided into separate trusts for his three children. The trustee of the revocable trust was also authorized in the beneficiary designation to create separate IRA accounts for each child, which was done after the decedent's death. The trustee duly created the three separate trusts for the children and no amounts from the IRA were ever paid to the initial, undivided revocable trust."

"Despite this, in an unfortunate example of form over substance, the IRS ruled that the separate account rules did not apply. The IRS stated that the separate trusts for the children were not created by

the decedent; rather, they had been created by the trustee after the decedent's death. The IRS viewed this situation as plan amounts passing through the original revocable trust, and concluded that the oldest child's life expectancy must be used to determine the minimum distributions for all the children's trusts. This reasoning would apply to your client's situation as well."

"So what can you do? It seems that the client must actually create the separate trusts under the revocable trust before the client dies. Perhaps the revocable trust can set up a trust for each heir's ultimate benefit now, fund it with \$10, and then have the revocable trust pour over into these separate trusts at the client's death. The IRA plan's beneficiary designation must provide that each of the trusts receive the appropriate fractional amount, rather than simply requiring that the proceeds be paid to the revocable trust. (Plan administrators and IRA custodians may need to start adding additional lines on their beneficiary designation forms.) Separate IRA accounts could also be used, but the beneficiary of each would still have to be a separate trust for the heir/beneficiary in existence prior to the client's death."

Asset Protection of Pension Plans:

- I. All ERISA type plans are asset protected under federal tax law:
 1. Where there are other employees besides the owner who participate in the company pension program.
 2. Excluding, however, protection from divorce/spousal and IRS claims.
 3. Asset protection even extends to most bankruptcy claims for ERISA plans.
 4. No additional asset protection planning can be implemented (nor is reasonably necessary) for ERISA plans.
- II. IRA plans are asset protected by laws of most states (list available at NAFEP). However, the amount which is protected varies from state to state.
 1. No additional asset protection planning can be implemented for IRAs (other than moving to a state with more protection). What is provided under state law is all that the plan owner can obtain.

SAFETY DEPOSIT BOXES

Safety deposit boxes are handled similar to the bank account arrangements. The trust can be named as a joint tenant/signer on an existing box, or a dedicated box owned by the trust can be rented. The main trust documents should contain information indicating where the safety deposit box is located, what it contains, and where the records and keys are kept. This will help the trustee to step in and take care of trust business when that is necessary.

CONVEYING REAL ESTATE

The exact method by which the real estate conveyance documents are created is critical. If the transfer is not handled correctly it may cause the title to become clouded or uncertain. An obscure title would most likely prevent or delay a future sale of the property. This could require court intervention to solve the problem. Problems with a clouded title can be extremely expensive and a time consuming nightmare.

The trustee/trust officer won't usually know all the real estate titling variations and special situations that can arise. Real estate titling is a whole field of expertise of its own. Therefore the grantors should have real estate conveyances done by an expert, such as a title company or real estate attorney. As one example of this professional need, no deed should be prepared until a title search and/or title report is done to ascertain the complete and true nature of the existing title. Only a title expert can do that. It is not that expensive in most cases to have the conveyance documents prepared by outside experts. Do not shortchange or defeat your trust's whole function by failing to get proper legal help in making real estate transfers.

Something extra you should be aware of is, most title insurance is transferable to a trust when the real estate owners or their families are the beneficiaries of the trust. Make sure to have this important service follow the real estate into the trust whenever possible.

Below is good information to help both you, the trust grantors, and the titling expert you hire to make effective real estate transfers to your Premier II.

Real Estate Transfer Taxes. Transferring ownership of real estate to a trust may cause a re-assessment of property taxes due to the county or state viewing the transaction as a sale. When a re-assessment is enforced it is usually due to the trust being irrevocable. Often times these re-assessments do not apply to transfers to irrevocable trusts where

the grantors or their direct heirs are the beneficiaries. In some states the transfer can cause substantial transfer taxes to be incurred, but using the right type of deed and/or language on the deed may prevent these taxes. Here again these are issues that require the counsel and help of local title professionals. Be sure to ask about this concern so the deed will be the correct type and include any special language that may be necessary.

Real Estate Deed Choice. To convey either developed or undeveloped real estate into a trust requires a deed. The type deed required varies from state to state. The most common are quit claim, warranty and grant deeds. Different states have their own variations of a given type deed and in conveyance procedures. Sometimes these variations are substantial. Also there may be special situations with any given property that causes some unusual requirement, and the above referred to transfer tax issue must be considered.

It is recommended that a quit claim deed not be used except for the following: The quit claim type is necessary to prevent tax re-assessments or transfer taxes. While quit claim deeds are commonly used to convey real estate into a trust, technically these deeds do not transfer title in all states. They merely release a claim that the signer may have on the property. It costs no more to use a warranty deed (or grant deed where applicable). Many times, however, the title company or attorney you hire will resist the usage of a warranty (grant) deed because of their fear of potential liability they may bear. But don't just take a simple brush off such as "Oh, a quit claim deed is fine, you don't really need anything else", or "we do quit claim deeds all the time, they work just fine". Press your request to get the best legal title possible. In the end, if you simply cannot get your expert to comply, find another expert or give in and use a quit claim deed. Quite honestly a quit claim deed will work just fine probably 99% of the time. But since it costs no more to use a warranty deed, why take a chance that your transfer will be among the 1% that fail?

Deed Conveyance Language and Recording. A trust has special requirements for the actual conveyance language that goes on the deed. The "Grantor", the transferor of the real estate, must use the full name and creation date of the trust that is to receive the property, and follow that with some special language about the trustee. Below are conveyance language examples for the most common trustee arrangements. Also, at the end of this "Setup and Operating Guide" are some sample deeds for further clarification.

NAFEP corporation as sole trustee:

to.... Friendly Home Trust, dated January 3, 2000, with XYZ Company, Inc., a Nevada corporation, as Trustee, said trustee and any successor trustee having full power to convey title....

(Friendly Home Trust and XYZ Company, Inc. are pseudonyms for the actual names. Get the real names from the trust document. The date used here is just an example.)

Private individual as sole trustee:

to.... Friendly Home Trust, dated January 3, 2000, with John Doe, of (City and State), as Trustee, said trustee and any successor trustee having full power to convey title....

Corp. + private individual as co-trustees:

to.... Friendly Home Trust, dated January 3, 2000 with XYZ Company, Inc., a Nevada corporation, and John Doe of (city & state) as co-trustees, said co-trustees and any successor trustees having full power to convey title when acting jointly....

Two private individuals as co-trustees:

to.... Friendly Home Trust, dated January 3, 2000, with John Doe of (city & state) and Jane Doe of (city & state) as co-trustees, said co-trustees and any successor trustees having full power to convey title when acting jointly....

Additional Recording Requirement. In addition to recording the deed at the County Recorder's office, it is recommended, sometimes required, that another document be recorded with the deed. This document may be referred to as either: Certificate of Trust, Affidavit of Trust or Memorandum of Trust in your state. NAFEP furnishes a version of this document with every trust, which is entitled "Affidavit/Certificate of Trust". A number of states require that either this document or the entire trust be recorded. But recording the entire trust is both expensive and is a compromise of privacy, and the affidavit/certificate of trust will meet all needs. So you will likely want to record only the affidavit/certificate.

The purpose of recording the affidavit/certificate of trust is to make certain there is a permanent and clear legal record for any future conveyance of the real estate out of the trust. In any future real estate conveyance out of the trust many title attorneys and title companies will require written proof of the trustee arrangements, trustee succession provisions, and powers of the trustee to convey title. The affidavit of trust provides that and other needed information for evaluation of the transferability of trust property.

Recording this information up-front removes all question concerning future transferability. There will be no problems later if trustees were changed (using proper trust procedures), if none of the original parties are around or if trust copies have been lost. Taking a long-term view of perhaps twenty to fifty years makes trust affidavit recording all but an absolute must.

Notify the Mortgage Company. If there is a mortgage on the real estate the lender's permission must be sought to transfer the property into trust. There may be a "due on sale" clause in the note that the lender could attempt to use to call the note if the lender did not give advance permission. Various state and federal laws prohibit the mortgage company in most cases from denying this permission for trust transfers for intra-family usage. The lenders rarely give any difficulty in granting permission, but if they do the law is on the grantors' side. The purpose of advance permission is to avoid a conflict or nasty surprise later over the lender's attempts to call the note.

Notify the Insurance Company. Be certain to notify the property and casualty insurance company that covers the real estate (or other property) before transferring the asset to the trust. Various insurance companies will handle the policy differently, but typically they will name the trust as an "interested party" or as a co-insured. Without this notification and change the property insurance may not be in force after the property is placed in the trust.

AUTOMOBILES, TRUCKS, RVs, ETC.

Retitling. Go to the appropriate state agency where auto titles are changed, and transfer the title into the name of the trust. If you explain that you are just changing the owner's name, and are not selling the vehicle, and/or that you are transferring the property into a family trust, most states will make the transfer without charging a sales or excise tax. There is usually just a nominal, transfer fee. However, some states may treat the transfer as a sale, even though no money changed hands, and even though the only difference is a name change. When this happens, it usually is because the trust is irrevocable. To help avoid this problem, the Holding Trusts are written with a revocable provision, which lasts for the first 30 days after property is placed into them. If the department or agency asks, you can truthfully answer that the auto is going into a revocable trust. If you cannot avoid a high tax on this transfer, consider waiting until you purchase your next vehicle, and then titling it in the name of trust from the beginning.

Mortgaged Vehicles. When there is a mortgage

on the vehicle, the lender usually holds the title or has a lien against it. In those cases, you have to approach the lender for assistance in getting the title transferred. Most large lending institutions are not customer friendly enough to help with this, though there is no legal or financial reason they cannot help you. They would still have a lien on the vehicle and its title after you changed the title to the trust name, but they usually remain opposed to helping you.

"Workaround" Solution for Vehicles. If problems with either the state vehicle agency or the lender prevent retitling the vehicle in the name of the trust, there is a workaround that still accomplishes asset protection and effective trust ownership. This can be done by placing a UCC commercial lien on the vehicle, naming the Primary Trust as the lien holder or assignee, and the grantor as the transferor or assignor of interest in the vehicle. All fifty states have a version of UCC liens, liens that are created for personal property (as opposed to real property). The lien should be written for a dollar amount which is sufficient to cover the highest amount of equity that the transferor expects the vehicle to ever have. If a creditor ever tries to take the vehicle with a judgment, they must first pay off any outside, first mortgages which exist against the vehicle, and then pay off the UCC lien, which is a second mortgage. This would leave the creditor with no way of clearing a gain on a resale of the vehicle, so they would probably not claim the vehicle. Even if they did, the trust would be paid for the stated amount on its UCC lien.

No Holding Trust is necessary to hold a UCC lien. The lien can be held directly by the Primary Trust. So it is wise to check out vehicle transfer issues before having a Holding Trust created for vehicle ownership.

Complete information on how to create and file UCC liens, along with an explanation of how they can be valid in this particular application, is available through your NAFEP Associate. He/she can provide NAFEP's training material on this subject from the NAFEP Certified Estate Planner training manual.

Leased Vehicles. Most vehicle leases will not allow the vehicle to be transferred into a trust, and few drivers have sufficient equity in their leased vehicle to be worth protecting or including in their estate planning. If the equity is deemed to be significant, the UCC lien procedure referred to above can be used and is an effective way to preserve and protect the equity.

Notify the Insurance Company. Be certain to notify your auto insurance agent that this change in ownership will occur. Usually, the best way to handle the insurance policy is to have the trust listed as an

interested party, co-insured or as an additional insured. If nothing is done with the insurance policy there may not be insurance in effect after the vehicle is transferred into trust. Rely on your insurance agent for the best way to handle this.

TRANSFERRING NOTES RECEIVABLES

Property that the grantors are carrying paper on, such as a Deed of Trust, note receivable, etc. may be transferred to the Primary Trust unless language in the paper prohibits a transfer. Even in that case you still may transfer the interest of that paper (the payments) to the trust. In both cases send a copy of the Deed of Trust and a notice to the payer directing him or her to henceforth send the payments to the Trustee in the name of the trust. Then use a bill of sale as the transfer document to move the ownership of the paper to the trust.

TRANSFERRING BUSINESS INTERESTS

To change ownership of publicly traded securities, generally use the information in the earlier topic with the heading "Financial and Brokerage Accounts". When you directly hold stock certificates, generally use this section for transfer information. However, *do not* place a personally owned business enterprise directly into any of the trusts of a Premier II. Use either a limited liability company (LLC) or a corporation to own and/or operate the business enterprise (see a NAFEP Associate for more information).

Proprietorships. As stated in the above paragraph, do not place proprietorship businesses in any part of a Premier II. You can, and probably should, put some of the business assets in Holding Trusts, such as business equipment, real estate and vehicles. But the operation and management of the business should be handled with a limited liability company or a corporation, and never by any part of your trust. This includes the management of rental real estate. Never manage real estate or collect rents in the name of your Primary Trust. Real estate management also should be handled by an LLC or corporation.

Corporate Stock. If you hold physical shares of corporate stock, as opposed to having them in a brokerage account, then the following instructions apply. Both C and S* corporation shares can be readily transferred to the Primary Trust. Generally, corporate shares are represented by certificates, with an assignment of ownership section on the backside of the certificate. After the assignment is made to the trust the shares normally would be turned in to the corporate secretary, who issues replacement shares

directly to the Primary Trust. See an appropriate business advisor, or the corporate secretary, for help in making the actual transfer. When the transfer is complete, be certain to keep copies or the originals of the reissued shares with the Primary Trust records.

* The special tax status of S corporations will not be compromised as long as the grantors are alive and are still the current trust beneficiaries. Even though the Primary Trust is irrevocable, it is also a "grantor" trust and Federal tax laws view the shares as still being held by the grantor(s). After the death of the last grantor, S shares in the trust will require sale or disbursement within two years, or the filing of a special "QSST" election.

Partnerships. Some or most partnership agreements will require permission of the other partners for one partner to make a change in the ownership of partnership interests. Normally the other partners will not have a problem with this when the new owner is a family trust. There is no uniform or standard procedure for transferring partnership interests though, so this Guide can only suggest you find an appropriate business advisor for help in making these transfers. Make all transfers of partnership interests to the Primary Trust, and keep copies of the paperwork with that trust.

BILL OF SALE DOCUMENT

A customized bill of sale is supplied for each Holding Trust, with a few blanks for the grantor to fill out. Use a bill of sale to convey untitled personal and physical property to the Holding Trust (or the Primary Trust in the case of the Premier LitE). You do not need a bill of sale for real estate, vehicles with titles, or financial accounts with banks, stock brokerages and other financial institutions. You also do not need to use a bill of sale or a Holding Trust for personal effects (handled by the "Disposition of Personal Effects documents) or household items (handled by the "Schedule A"). Common personal property items requiring a Holding Trust and a bill of sale include things such as: untitled business and other equipment (like computers, manufacturing equipment, etc.), un-titled vehicles (such as small watercraft and snowmobiles), and possibly guns (though these are usually handled with the "Disposition of Personal Effects" document). These items are "personal" whether they belong to an individual or to a business.

If there isn't enough room on one bill of sale to list all the property going into the trust, you can do one of two things. (1) Make additional copies of the bill of sale before you enter any information on the original, then use multiple copies to list all the assets, or, (2) list the property on a separate sheet of paper and

attach it to the bill of sale. Then in the "Assets Conveyed" blank on the bill of sale, write in the words, "See Attached List". Then, have the trust officer and the grantor initial the attached list.

Filling out the notary section is optional, but doing it does make a slightly better legal document.

The bill of sale does not need to be recorded with the County Recorder. Simply keep one copy with the trust documents, and one in the trustee's files.

SPECIFIC GIFTS OF PERSONAL ITEMS

The gifting of personal effects to specific heirs is handled with a two-part document. The first part is called "Bequeath of Specific Gifts", and the second is the "Memorandum Of Disposition Of Personal Effects". There is a pair of these documents furnished for each grantor with each Premier II trust. They are very simple to understand and implement.

The Bequeath document grants personal items to the ownership of the trust with a life estate interest being retained by the grantor in the personal effects. After the grantor dies, the trustee will use the "Memorandum" to transfer the personal effects to the proper heirs. The grantor retains the power to change the list of effects and the beneficiaries at any time, and as often as he/she wishes. Before using the "Memorandum" document make copies of it so that you can fill out new versions in the future. Any time you do this mark the old one "Void", very clearly or just throw all original copies away.

This keeps control and usage of the effects with the grantor, and allows total freedom to select and change heirs for these effects. But, since they are conveyed to the trust these items will avoid probate. This process, especially when handled by an independent trustee, will also help a great deal in eliminating intra-family quarrels over these items. Please read the complete text of the "Bequeath" document.

COMMON HOUSEHOLD ITEMS

Property such as furniture, kitchen items, wall decor, fixtures, electronics, etc. are listed generically on a document furnished with the Primary Trust, entitled "Schedule A". Simply signing this document and keeping it with the Primary Trust records is an effective transfer of these items to trust ownership. This is effective for both transferring these items to the eventual heirs of the grantors, as well as protecting them from lawsuits and creditors. As simple as the document is, it will stop a creditor from taking these items in satisfaction of a judgment. The

list is broad enough to include virtually anything of value found in the average home, but there is room on the Schedule to list anything specific where necessary.

Do not rely on this Schedule to transfer personal effects and family heirlooms to specific heirs. That should be done with the "Bequeath of Specific Gifts" document referred to above.

STEP-BY-STEP TRUST SETUP

The steps below, are simplified, initial setup instructions. Detailed information on these steps is contained in the preceding pages of this guide. Perform these steps in the order listed:

1. Open Primary Trust bank, investment and savings accounts if any are required.

- A. Retain the initial deposit slips and/or account statements with the Primary Trust. This provides proper record keeping.

2. Convey real estate to appropriate Holding Trust(s). (Also see the "Conveying Real Estate" and "Privacy and Secrecy" topics of this guide.)

- A. Contact mortgage companies first for written approval to change ownership of real estate.

- B. When approval is received, change ownership and title to the name of the appropriate trust(s), using preferably a warranty (or grant) deed, and handled by a title company.

- C. Notify insurance agents of change in ownership.

- D. Record deeds and a copy of the Affidavit/Certificate of Trust (optional) at County Recorder's office, in the same county where the property is located.

- E. When the recorded deeds are returned by the county, retain them with the appropriate Holding Trust documents.

3. Convey personal property and vehicles to appropriate Holding Trusts. (See the "Automobiles, Trucks, RVs, Etc." and "Bill of Sale" topics of guide.)

- A. Make an inventory of equipment, untitled vehicles (and possibly guns) that go into trusts. Do not include items that are listed on the "Disposition Of Personal Effects" or Schedule A documents. Generally speaking, exclude

items worth less than \$250.00.

B. List the above items on a bill of sale (furnished with each Holding Trust). If the items are too numerous, attach separate lists of the items to the bill of sale as an exhibit, or use several bills of sale.

C. Get bills of sale signed by grantors and trustee/trust officer. Retain completed bill(s) of sale with the appropriate Holding Trust documents, and with trustee.

D. Vehicles. Notify insurance agent, in advance, of the title change and of the upcoming name change. Change vehicle titles to appropriate trust name, and retain new title with that trust.

CHAPTER 4. OPERATING A FUNDED TRUST

BORROWING, LENDING, PLEDGING ASSETS, HIGH RISK INVESTMENTS

It may become necessary to pledge trust assets to an outside lender due to a need of the grantors to borrow money. As long as the borrowing is prudent and does not damage the interests of the beneficiaries, the trustee should normally approve and sign the note which pledges trust assets as collateral. Borrowing money for the purchase of a home, home improvements, automobiles or other asset purchases (especially if the new asset is going into one of the trusts), consolidation of debt against trust assets, etc., are examples of normal activities in trust estate management. Either borrowing or spending trust money to purchase a new trust asset does not constitute a damage to the trust assets or a removal of trust principal. Either of these activities are normal and appropriate when done in a prudent manner.

Problem Lending. An example of problem lending is: Trust funds are going to be either lent to, given away, or used in behalf of someone who is an outsider to the trust structure, and/or who has insufficient collateral or credit worthiness of their own. Problem borrowing would be receiving an unsecured loan from the trust, or making trust loans to use for purposes that have little or no chance of enhancing the estate. Poor creditworthy borrowers and non-collateralized loans are high-risk loans, which a "prudent" person would not make. ("Prudent" person is a legal principle that the trustee should follow to comply with his/her fiduciary responsibilities.)

High Risk Investments. Likewise, a prudent person does not make high-risk investments. (The description of "high risk" investments is beyond the scope of this publication.) Generally, the trustee is safe in investment selection by taking one of the following measures:

1. Making the grantors the investment account managers.
2. Asking for or adhering to the investment choices and desires of the grantors or other adult and current beneficiaries.
3. Hiring in good faith a licensed financial advisor to make the trust investment decisions and recommendations.

A licensed financial advisor in this sense is one that has minimum licensing from both the SEC and from the state's securities agency, which will permit the advisor to recommend individual securities and mutual funds.

Trustee Measures. The trustee should never initiate borrowing, lending or investments that have a significant potential to degrade the trust estate, to lose money. The Primary Trust language allows, but does not require, the trustee to engage in some high risk activities if they are requested by the grantors or other current beneficiaries. If a high-risk activity is requested and the trustee independently decides to consent, the trustee must take special precautions to protect himself from personal liability in the event there is a financial loss. This would entail the trustee getting written documentation of the request, with signatures, from the requesting parties. If the trustee cannot arrange this precaution, he or she should refuse to assist with such deals, because the trustee may be required to answer, financially and personally, to the beneficiaries if the deal goes bad. Also, any loans that are made from the trust must be at normal market interest rates and terms. Anything less may constitute a non-prudent loan or investment, leading to the trustee's personal liability. If a loan is made to the grantors, market interest rates are important to keep asset protection in place. A below market rate loan to the grantors could be construed as the grantors' taking trust principal for personal consumption.

FINANCIAL STATEMENTS AND CREDIT HISTORIES

Financial Statements. In many cases the grantors will want to produce personal financial statements that include all trust property in the list of assets on their financial statement. This is legal and proper provided that the financial statement contains a footnote notation on the asset list with footnote language something like the following: "Assets held in trust for my/our benefit". This notation is proper because the grantors have not given up their economic interest in the assets, they have only given up the legal title. Since they continue to own the economic interests they may properly value those interests (the assets) on a personal financial statement. If they do not include the footnote, they risk losing asset protection (by claiming full ownership of the assets on the financial statement). They also risk possible charges of fraud if they use the financial statement to obtain a loan without disclosing the status of the title of the assets (held in trust). However, the existence of the footnote should not inhibit the grantors' ability to use the financial statement to obtain credit. In fact, as outlined in the

prior topic, where needed the trustee should comply with prudent pledging of trust assets for loans which do not place an unusual risk on trust values.

Credit Histories. It is also proper and possible to establish credit under the Primary Trust, and to produce a financial statement for the trust, rather than personal financial statements for the grantors. The Primary Trust can properly report the assets in the related Holding Trusts as its own asset for accounting purposes. This type statement is referred to as a "combined financial statement". It is possible for the trust to borrow or lend money, and to pledge assets for any prudent purpose, though those activities should be approved and supervised by the trustee. Since the grantors own a life estate in the property, and receive any trust income, they would most likely be required to co-sign on any trust loan, pledging their interest in the property.

Many creditors will automatically extend some level of unsecured credit to the trust. The creditors who would do this include: utility companies, office space providers or landlords, office and janitorial supply companies, equipment rental or lease companies and local and long distance phone companies. Some of this credit activity will be reported to credit rating bureaus, or will at least be available for future creditors to check on. So, if the credit is paid as agreed, these reports will help to build future and larger credit possibilities.

Important Note: As thoroughly outlined in Chapter 2, do not allow the Primary Trust to engage in a business enterprise. Do not allow the Primary Trust to be involved in any activity that could lead to a lawsuit against this trust. The Primary Trust owns the entire estate of the grantors, both directly and indirectly as the beneficiary of Holding

Credit may be established in the trust by making asset purchases on credit. For example, any new asset purchase may be bought in the name of the Primary Trust. Where necessary, the grantors or one of the beneficiaries can personally guarantee the payments. But, the loan can name the trust as the borrower. With most vehicle, equipment and consumer loans the credit activity will be automatically reported to credit rating bureaus. Paying the loan payments as agreed will generate positive credit reports for the trust.

Another step that may be taken is to get existing loans converted from personal names to trust names. If the grantors place property in trust that has a loan

on it, many lenders will be willing to change the name of the borrower on the loan as long as the grantors remain as loan guarantors. Again, if these loans are paid as agreed, positive credit reports will be generated. The best loan candidates for this usage are consumer loans on items such as homes, vehicles, furniture, appliances, electronics, etc.

To obtain a credit card in the name of a trust, the grantor or a beneficiary may personally guarantee the payments. If that cannot be done, some credit card providers will agree to issue a card that is secured or guaranteed. This type card requires a certain amount of cash to be deposited up-front with the credit card issuer. The up-front cash acts to secure or guarantee that the card company can get their money if the payments are not made. Even though the payments are secured, prompt payments are still important. This will help to create positive credit reports, and that can lead to the cash deposit being returned and to other credit becoming available.

BOOKKEEPING

Once the grantors die or become incapacitated the trustee has a legal liability to maintain bookkeeping for the purposes of annual reporting to the beneficiaries. During the active lives of the grantors they must assist the trustee in keeping up with what is in the trust and what activities are going on. The grantors often receive all trust financial statements, for example, and often handle any trust check writing and deposit activity. The grantors may place additional assets into the trust without the trustee's immediate knowledge. In order for the trustee to competently fulfill his role on the death or incapacitation of the grantors, the trustee must receive at least one copy per year of financial statements and records. The Trustee must also be up to date with a list of trust assets (and debts or other liabilities). So in addition to financial statement copies, the trustee needs a copy of all deeds, titles and bills of sale for physical assets in the trust. The trustee needs records regarding life insurance policies, annuities and pension plans which name the trust as either or both owner or beneficiary.

Some of this bookkeeping requirement is necessary to keep asset protection in place. If the grantors are managing trust financial accounts, they will want to be able to prove that they did not remove principal from the trust without going thru the proper steps (see Chapter 2). Good bookkeeping will be necessary to provide this proof when and if necessary.