

ESTATE PLANNING NEWS



Incentive Trusts:

Trusts Can Pass On Values, Not Just Valuables

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For generations, Americans have used trusts to transfer wealth to their descendants. Oftentimes, trusts are created by parents who hope to secure a comfortable lifestyle for their children. Recently, though, more Americans have begun to fear something other than the prospect that their children will not have enough: They fear they will have too much.

Inheriting Too Much Wealth Can Be Bad

The notion that inheriting too much wealth can be bad for a child is not new. In an 1981 essay entitled *The Advantages of Poverty*, Andrew Carnegie wrote that “the parent who leaves his son enormous wealth generally deadens the talents and energies of the son, and tempts him to lead a less useful and less worthy life than he otherwise would.” (cont. on page 3)

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Announcements

Happy New Year! I wish you and your family a healthy and prosperous 2007 and hope you had a wonderful holiday season.

To celebrate the close of 2006, my husband and I toured three Eastern European cities: Prague, Vienna and Budapest. The picture on the right was taken in an ornamental gateway in Buda's Castle District, steps away from the Royal Palace.



Tip of the Month

Incorporate Charitable Giving Into Your Estate Plan

In addition to writing a check today, there are many ways to include your favorite charity in your estate plan:

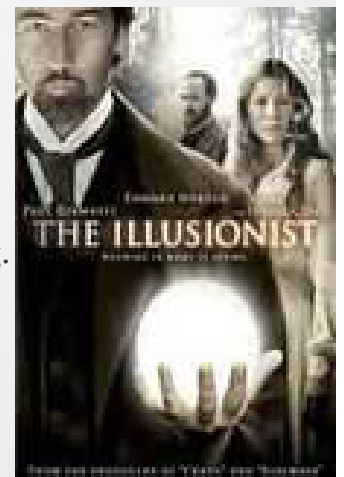
- 1) Provide that a cash gift, or percentage of your estate, be distributed to charity upon your death;
- 2) Create a discretionary trust for a loved one, then name a charity to receive the balance when the trust ends;
- 3) Specify that, instead of the State of California, one or more charities will benefit if no heirs survive you; or
- 4) For greater tax savings, establish a charitable lead or charitable remainder trust.



Entertainment

The Illusionist (2006)

Set in early 20th century Vienna, this romantic thriller centers on illusionist extraordinaire Eisenheim (Edward Norton), who falls for an aristocrat (Jessica Biel) well above his social standing. When she becomes engaged to Crown Prince Leopold (Rufus Sewell), the master magician employs his powers to win her love. His daring scheme creates tumult within the monarchy and ignites the suspicions of Chief Inspector Uhl (Paul Giamatti).



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The perfect amount to leave children is enough so they would feel they could do anything, but not so much that they could do nothing.

-- WARREN BUFFETT

Incentive Trusts

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More Americans Are Millionaires

A 2005 survey conducted by market information company TNS revealed that a record 8.9 million U.S. households enjoy a net worth in excess of \$1 million. This marks an 8% increase over the same figures for 2004, which were in turn a 33% increase over the figures from 2003.

Multimillionaires are also increasingly common. Internal Revenue Service data reveals that, from 1980 to 2000, the number of Americans with seven figure annual incomes increased more than tenfold, and in 2000, there were more than 20 times as many American billionaires as there were in 1982.

While inflation is responsible for some increase in wealth, the fact remains that being rich is less unusual today than it was in the past.

Affluent Parents Worry That Wealth Will Negatively Impact Their Children

How do millionaire parents feel about leaving such great wealth to their children? The U.S. Trust Survey of Affluent Americans, generally regarded as an unbiased barometer of the opinions of wealthy individuals, revealed that more than half of affluent parents are concerned that their children "will place

too much emphasis on material possessions," "will be naive about the value of money and how hard it is to earn," and "will spend beyond their means." Almost half worry that their children "will have their initiative and independence undermined by having material advantages."

Parents who earned their fortune through hard work may follow the lead of Warren Buffett, who last summer announced plans to give the bulk of his vast fortune to the Bill and Melinda Gates Foundation.

Other parents may prefer to leave money to their children with strings attached.

Growing Popularity of Incentive Trusts

Using a trust, parents can limit distributions to their children in a way that will encourage positive behavior. Traditionally, the trust would be structured as a discretionary trust, where the trustee has authority to decide how the money will be spent, and the trustee rewards conduct that would have met with the trust maker's approval.

Recently, however, incentive trusts have grown in popularity.

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An incentive trust is an irrevocable trust intended to foster responsibility and social consciousness in its beneficiary. Incentive trusts include one or more goals that a child must satisfy in order to benefit from her family's wealth. Conditions tend to be based on academic, moral and professional achievements.

Rewarding Positive Behavior

1) Encourage Education

The most common incentives: a) grant the trustee discretion to pay funds to a child (or third party) for tuition, books, room and board; and b) award some amount of trust income or principal to a child who graduates from college. A trust may also provide funds to a child who completes high school or receives a graduate degree.

Raising the bar, parents could require their children to obtain a certain grade point average, enroll in the family alma mater, or study a specified subject.

2) Moral Incentives

Some parents are using incentive trusts to promote a particular lifestyle. Typically, these provisions encourage commitment to family and discourage substance abuse. So long as the parents' morals are consistent with public policy, they may reward marriage, penalize divorce, promote procreation, or even offer a financial incentive for a child (or the child's spouse) to stay at home with the grandchildren.

Other parents encourage their children to contribute to charitable causes. A trust may distribute funds for philanthropic efforts (e.g., pay a salary to a child who joins the family charitable foundation) or grant matching contributions.

3) Promote a Productive Career

Many parents, who want their children to work hard, use incentive trusts to reward productivity. Under an "earn a dollar, get a dollar" arrangement, a trust can pay a child a dollar for every dollar that the child earns on her own. Alternately, to promote savings, payments may mirror dollars saved, rather than dollars earned. Another variation would require a child to earn a certain amount of income or achieve a specified net worth, thereby ensuring that the trust's assets will be passed down to subsequent generations.

Conclusion

Incentive trusts are growing in popularity among parents who wish to pass certain values on to their children. Nevertheless, incentive trusts are not right for every family, and consideration should be given to the possibility that a child will not -- or cannot -- satisfy a specific condition. With the assistance of a qualified estate planning attorney, parents may anticipate potential circumstances and create a more flexible instrument that stands the test of time.

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