

# Quick Probates: An Oxymoron?

## Virginia Act Changes Time-Consuming Process for Small Estates

The Virginia Small Estates Act allows a relatively quick and easy way to handle estates with personal property probate assets of \$50,000 or less. If an estate qualifies under the Virginia Small Estates Act, then it can avoid the more formal and time-consuming probate process. The initial important issue here is what constitutes a "probate asset," because many assets of a decedent pass directly to survivors without going through probate at all.

Generally, the kinds of assets that pass directly to survivors and do not go through probate are:



- Life insurance (paid directly to the named beneficiary, usually the spouse or children);
- Property owned jointly with rights of survivorship (usually jointly owned bank accounts, jointly owned real estate between husband and wife); and IRAs and 401(k)s (paid directly to named beneficiaries, usually the spouse or children).

So what kinds of assets do go through probate and constitute a "probate asset?" Generally, those are assets that are titled solely in the name of the decedent, such as:

- Bank accounts titled in the decedent's name alone; and
- Stocks and bonds titled in the decedent's name alone.

If the probate assets total \$50,000 or less, the decedent's successor may present an affidavit containing certain information to whomever holds the probate asset, in order to take control of that asset for proper distribution. That affidavit would include the following:

- That the value of the decedent's entire personal probate estate, wherever located, does not exceed \$50,000;
- That at least 60 days have elapsed since the decedent's death;
- That no application for the appointment of a personal representative for the decedent is pending or has been granted in any jurisdiction;
- That the decedent's will, if any, has been probated and the list of the decedent's heirs was duly filed in the Circuit Court Clerk's Office; and
- That the claiming successor is entitled to the requested payment or delivery and on what basis.

In addition, statutes provide that a bank or credit union may pay to the decedent's successor without an affidavit any balance of the decedent that does not exceed \$15,000. There are also several other statutes in Virginia that allow certain entities to distribute assets to the successor without probate within certain limits.

For those estates with probate assets of \$50,000 or less, the Virginia Small Estates Act is a helpful mechanism that has simplified the often-times long, drawn-out process of probate.

## Cohen and Burnett, P.C. Legacy Analytics, LLC



WINTER 2008



FOUNDING PARTNER

**I. Mark Cohen**  
**JD, LLM & CFP™**

As the year draws to a close I am looking back on what turned out to be a very full year. Our firm continues to grow and prosper. We added several very talented employees and I published several articles. The BNA portfolio on the Uniform Trust Code should be coming out in February. My part is done. We are just waiting for BNA to do the copy edit and then on to production.

Michael is now a freshman in the College of William and Mary and doing very well. Compared to the rigors and stress of his high school, his first semester in college is somewhat of a relief - only four classes and he's doing very well in all of them. He fills up his considerable free time with AEPi fraternity activities and is running for an office in the Hillel Club. Rachel, of course, is in the midst of her senior year at Marshall High School where she is taking six IB classes, two non-IB classes, is in band and on the swim team. I am pleased to announce that she was just admitted to the College of William and Mary by early decision. Soon we will have both our children there. Kathy just finished her class in Italian for tourists, and I hear that Thanksgiving week is a great time to visit Italy. I hope the dollar gets a little stronger before we travel to Europe.

For those of you who are following my efforts towards the Marine Corps Marathon I regret to say that I managed to injure my left foot while training. The doctor told me not to run until January at the earliest. Thanks to your generosity, however, we did accomplish the larger goal of raising over \$3,300 to benefit the Leukemia and Lymphoma Society.

**Best wishes for a happy holiday!**

### In IRA We Trust

#### *Designating Trusts as Beneficiaries*

I probably get this question more than any other. "If I name my trust as the beneficiary of my IRA, will my beneficiaries be able to stretch the payout over their life expectancies?"

Before I answer this question, let's review some of the basics about IRA beneficiaries and distributions. Also, remember that this article is generic and not intended as specific advice to anyone, and if I were to cover the exceptions to everything I write here, I would fill up this newsletter and the next three.



First, funds that remain in the IRA are not taxed on their income or growth until they are withdrawn, at which time they are reported as ordinary income. If you withdraw IRA funds before you are age 59 ½ then you must also pay a 10% penalty. Because of this adverse income tax implication, most of our clients will want to leave their funds in the IRA as long as possible. The law requires, however, that once you reach age 70 ½ you must begin withdrawing funds from your IRA in amounts that are calculated to exhaust the IRA at your life expectancy. For example, at age 70 ½ the IRS tables say your life expectancy is 16 years, so you must withdraw one-sixteenth of the balance that year. At age 71, however, your life expectancy is 15.3 years so you must withdraw 1/15.3 of the balance that year.

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Historically we wrote and mailed the newsletter by the 15<sup>th</sup> of each new calendar quarter. We have decided going forward to complete and mail it closer to the end of each calendar quarter, roughly 15 days earlier. We hope you find it valuable to read it as this is all written and edited by our firm.

We continue to prepare for our move this coming April to the second floor office condominium in this same building. George Reilly returned to his job with the Navy Judge Advocate General where he will put many lessons learned with us to good use helping our soldiers and sailors with their legal problems. Andrew Vanderhoof joined us two weeks later having left his long-standing job with the legal and tax publishing firm, the Bureau of National Affairs, where he was an editor for estate, gift and related tax matters.

On the family side, my wife, Barb, is back in school and maintaining a slightly better work-sleep ratio with the same number of classes but fewer class preparations. She is no longer the MathCounts Coach at Longfellow Middle School, where they were twice National Champions in seven years, but instead is on the Board of Directors for National MathCounts. Our children are doing exceedingly well. David got word in November that he has passed the NY Bar so he is a full fledged attorney with his NY law firm loving his work that often goes past midnight. We spent one weekend with him in November strolling Fifth Avenue, visiting the Met and eating some fascinating meals. Edward is home frequently when his ship is in port working on his contacts at the State Department, Department of Defense and national intelligence organization as he readies for transition to civilian life in May. We saw Jennifer in October at the University of Louisville where she is working on her PhD. That downtown area is far more attractive than I remember from decades ago. We also found out how hard it is to get a ticket to the Kentucky Derby at Churchill Downs.

For myself, I am not climbing any mountains this quarter or doing any long rides or races. I will settle for the daily recreation center work outs and wait for warmer weather. This Thanksgiving we had nine for turkey dinner. After Christmas, we have thirteen family members converging on Eden, Utah to ski, snowboard or just plain goof off.

**Happy Holidays and Happy New Year.**

## “Kiddie Tax” Age Changes

At one time, wealthy parents could significantly lower their family’s tax bill by transferring investment assets to their minor children. This worked by taking income out of the parents’ higher tax bracket and placing it in the lower tax bracket of their children. For years this was done by transferring securities into Uniform Gift to Minors Act or Uniform Transfer to Minors Act (UGMA/UTMA) accounts for the child(ren). To curtail the use of this tax short-cut, Congress enacted the “Kiddie Tax” rules.

Unearned income of minors in excess of \$1,700 is currently taxed at the parents’ rate for kids under age 18. In tax year 2008, the age rises to 19 (or 24 for full-time students).

This age expansion will have ramifications on the UGMA/UTMA accounts, which is a popular college savings vehicle for many people. The UGMA/UTMA strategy is to transfer growth investments which don’t usually throw off much income, to a child’s account. Income below the ceiling is taxed at the lower tax rate for children. Once the child passes the “Kiddie Tax” age limit, they are taxed on the income at their own marginal tax rates.

The new rule extends the “Kiddie Tax” rate to children who are college age (19) or full-time students (up to 24).

You should consider this in your tax planning for your children’s college education.



## In IRA We Trust: *Designating Trusts as Beneficiaries*

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These Required Minimum Distributions (RMDs) must be taken out each year for the rest of your life. If you miss a RMD, you will pay a penalty of ½ of the amount you should have taken out, and then you will still have to take out the RMD that you missed. The rule only applies to the *minimum* required to be withdrawn from the IRA. You can always take out more. However, unless you need the IRA funds, your goal is to take out as little as possible each year to save income taxes.

*Recalculating vs. straight line.* Did you notice that the life expectancy of a 70-year old is 16 years but that of a 71-year old is 15.3 years, not 15 years? That is because each year that you live buys you additional life expectancy. For example, when you reach age 86 (the life expectancy of a 70-year-old) you still have about 6.5 years of life expectancy. Because of this feature of the life expectancy tables, you are allowed to recalculate your life expectancy each year. You want to do this because it will reduce your RMD and save you taxes. In some cases, you cannot recalculate life expectancies and must simply reduce the life expectancy by one year each year. This is known as a “straight line” computation of life expectancy.

So far, I have explained a simple case where there is one owner of the IRA and no beneficiary designated on the IRA form. What if a beneficiary is designated on the form (the “Designated Beneficiary”)? The only difference is that now the life expectancy calculation is based upon the Joint and Survivor life expectancy of you and the beneficiary. If you are age 71 and your spouse who is the designated beneficiary is age 70, the IRS tables tell us that your joint and survivor life expectancy is 20.2 years. Thus, your RMD is a 1/20.2 of the balance that year. The following year your joint and survivor life expectancy is 19.4, so the RMD is 1/19.4 of the balance in the IRA. Because the spouse is the designated beneficiary, we can continue to recalculate life expectancies.

When you die, the IRA must continue to be paid out each year, but the RMD is now based upon the beneficiary’s life expectancy. If the beneficiary is your spouse, there are a number of interesting choices, but the vast majority of spouses do a “spousal roll over” and make the IRA their own. When the beneficiary is not a spouse then the beneficiary must continue to take out the RMD, but it is now calculated based upon the life expectancy of the

beneficiary at the time of the IRA owner’s death and then reduced by one for each year thereafter. Thus, a non-spousal beneficiary cannot recalculate life expectancies and must go with the straight-line method.

What if there are multiple individuals designated as beneficiaries such as “my children?” In that case there are two choices: (i) the life expectancy of the oldest member of the class of beneficiaries (your oldest child, in this example) is the measuring life for calculating the RMD; or (ii) the IRA is split into multiple, equal IRAs each with a separate child as the designated beneficiary. This second choice was recently clarified by the 2006 Pension Act, but only applies to a class of individuals, not a trust. How about a deadline to spice things up? The “designated beneficiary” is irrevocably set by September 30 of the year following the year of death. So, the paperwork splitting an IRA among multiple beneficiaries must be completed by that date.

This brings us finally to the original question – what if a trust is the designated beneficiary? If the trust does not meet the requirements of a “see through” trust then the IRA amounts must be paid out immediately. A “see-through” trust is one that is irrevocable when the payments are to be made to the beneficiary, and that has an individual as a beneficiary. *There also is a notice requirement that must be made by the same 30 September deadline to the custodian of the IRA!* Most of the trusts we write will qualify as a see-through trust. If so, we can look to the beneficiaries of the trust to determine the life expectancy for RMDs, but if there is more than one beneficiary, we must use the oldest member of the class for fixing the life expectancy.

Why designate a trust as the beneficiary? The trust has more flexibility to deal with unexpected situations such as a beneficiary’s death or divorce. It has provisions that address payments to young children or disabled persons. Also, although the IRA is protected from creditors while you are living, there is no assurance that creditor protection will be available to your beneficiaries after your death. Virtually every trust we have written provides protection from creditors.

So the short answer to the original question is – *yes*. If you do the math, you’ll see that a trust is a viable beneficiary.

