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Liquidating a remainder interest: simplifying personal finance

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Abstract

There are many ways in which decedents leave property in trust for their heirs. One technique is to grant a life estate to surviving children. The purpose of this paper is to describe verbally, and through example, an approach to liquidating a life estate. This simplification in personal finance involves a "buyout" of the interests of the remaindermen. The result is dissolution of the trust, leaving the income beneficiaries to manage, as owner in fee, the remaining assets as they wish, without the expense and complexity associated with maintaining a trust. © 2000 Elsevier Science Inc. All rights reserved.

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1. Introduction

There are many ways in which decedents leave property in trust for their heirs. One technique is to grant a life estate to surviving children that allows them to reap the income thrown-off from trust assets while, for all intents and purposes, leaving the corpus intact for later distribution to those with a remainder interest. The latter are usually the settler's (grantor's) grandchildren, but, in some instances, the settlor may choose to name charitable/tax-exempt organizations (for example, educational institutions) as the remaindermen. While

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such perfectly acceptable estate planning methods benefit younger generations and, eventually, a favored charity, they do involve complexity and expense.

Among such complications and costs one would include appointing and compensating trustees. Moreover, in their fiduciary capacity, these trustees must hew to the investing wishes of the grantor of the trust, which may not be in the best interest of the income beneficiaries. Furthermore, fiduciary tax returns must be prepared and submitted annually. Additionally, trust income tax brackets are much more compressed than the income tax brackets for individuals and, as a result, the highest rates are quickly reached unless most of the income is distributed to the income beneficiaries. Finally, in some instances, there may be a directive to hold the trust's financial assets with yet another party, such as an investment firm, incurring even greater expense.

The purpose of this paper is to describe verbally, and through example, an approach to liquidating a life estate in situations where the income beneficiaries are capable of managing the corpus of the trust and to demonstrate that this can be done to the mutual benefit of both the income beneficiaries and the remaindermen. This simplification in personal finance involves a "buyout" of the interests of the remaindermen using but a portion of the assets of the trust as payment. To put it formally, the income beneficiaries purchase all of the remainder interests in the trust. The result is dissolution of the trust, leaving the income beneficiaries to manage, as owner in fee, the remaining assets as they wish, without the expense and complexity associated with a trust.

2. A brief review of some relevant literature

While the body of literature relating to the specific issue discussed in this article is sparse, there are tangential discussions on liquidating a remainder interest and charitable remainder trusts.

In his article on charitable remainder trusts (CRT), Fooden (1996) notes that a CRT ". . . provides a mechanism for the transfer of property from one generation to the next without incurring any gift or estate tax liability." Moreover, the author observes that it is the only method for transferring the full value of "Highly Appreciated Assets" to heirs. In the same vein, Moyers, Spiegel and Baum (1997) state that in order to receive a higher tax benefit, the tangible appreciated person property (TAPP) CRT procedure should be taken into account ". . . when a client has valuable, low-basis tangible personal property that cannot be liquidated without incurring substantial capital gains." At the same time, each situation is unique regarding a remainder interest or trust and should be individually evaluated to find the option providing the greatest financial benefit and smallest tax consequence.

Siegel and Swerdlin (1996) consider the situation where the interests of the income and charitable beneficiaries of a trust do not overlap. The distinctive tax structure of such "split-interest trusts" allows a fiduciary to ally the wishes of the parties by investing for capital appreciation instead of income. This technique results in higher after-tax income to the donor (income beneficiary) and an anticipated gain to the charity.

In his article on selling a remainder interest, Croman (1994) states that a sale of a remainder interest could also reduce the estate taxes to be paid while still carrying out the

wishes of the decedent. The sale, which involves the payment by the buyer of the full value of the remainder interest, either in cash, exchange of property, a promissory note or an annuity, is recommended as a possible estate planning process.

Of course, the IRS has created regulations and recommendations to be followed regarding the liquidation of remainder interests and trusts. Herman-Giddens (1998) discusses the Proposed Regulations issued in 1997 by the IRS. They include matters related to ". . . flip unitrusts, the time for paying the annuity or unitrust amount, appraising unmarketable assets, . . . special valuation rules for CRTs, and prohibiting the allocation of precontribution capital gain to trust income." Many of the regulations are aimed at reducing abuses to the system; however, they will not seriously limit or impede planning by a donor who has a "genuine charitable intent." (Since implemented, these regulations are cited under *Treasury Regulations* and *United States Codes* in the References.)

While it would be impossible to affix an exact figure to the number of instances in which the "buyout" option should be considered, it can be said that anytime there are remaindermen other than family, typically charities and/or educational institutions, named in the trust this alternative may very well be appropriate.

Finally, although other contributions in this arena have addressed the possibility of valuing remainder interests, there has been no consideration of actually carrying out the process in practice and then convincing the remaindermen to accept a negotiated amount. This work meets both goals, dealing with many of the potential idiosyncrasies and difficulties attendant to the procedure.

3. Estate planning goal

The goal is to greatly simplify a complicated financial arrangement by changing it from an expensive, complex set of split interests (a subset of present interests and another subset of future interests in a long-term trust) into outright ownership. To accomplish the goal, it is necessary to convince the remaindermen that it is in everyone's best interest to liquidate the trust.

4. General method

4.1. Entering negotiations with the remaindermen

There are several steps that must be carried out in implementing this strategy of liquidating a trust. Without a doubt, the most crucial of these is the preparation and delivery of a thorough and easily understood explanation of the proposal to the remaindermen. It goes without saying that the efficiency of this process is inversely related to the number of the remaindermen and directly correlated to their level of financial sophistication. Institutional remaindermen can generally be counted on to have a current understanding of the technique and to readily assimilate the nuances of a particular situation. In contrast, individual remaindermen may find the approach difficult to comprehend initially, although most will

quickly appreciate that receiving something of value now could be worth as much or more than receiving a greater, but perhaps more uncertain, amount in the future. Individual remaindermen must also factor in their own mortality, something that charitable institutions can ignore.

How does one provide and convey an understandable interpretation of the "buyout" option? Most likely it will be initiated through the mail, followed by numerous telephone conversations with the remaindermen and/or their representatives.

The content of the initial communications with the remaindermen is likely to be most productive if it includes:

- How many other remaindermen there are and a promise to eventually reveal (assuming negotiations progress) whom the others are.
- The nature and the present value of the trust's assets.
- What proportional share of the trust's assets each remainderman is to receive. For example the letter might state:

> You are one of four remaindermen, each with an equal share. The value of the trust is approximately $1,400,000. Thus each remainderman's interest would be $350,000 (25%), if the income beneficiaries died today.

- Specific information about the income beneficiaries' interests and general information about the income beneficiaries themselves.
- A disclosure of any circumstances under which the income beneficiaries can spend trust principal (i.e., corpus).
- The grounds for opening negotiations and the arguments for accepting a reasonable "buyout" offer, rather than waiting for the trust to run its course. For example:

> The trust allows distribution of principal to the income beneficiaries to provide for entry into a profession or business. "A" is in his early fifties and "B" is in her late forties. The temptation to draw out the corpus of the trust to start a business is quite strong. There is nothing in the trust document itself that would prevent them from using trust funds to purchase a business, manage it for a reasonable period of time, and then sell it. There is no requirement that proceeds from the sale of the business be put back into the trust.

Early in the negotiations, the income beneficiaries' representative should include a "sanitized" copy of the trust document, that is one that blacks out the identity of the settlors, the trustee, and the individual beneficiaries. This will allow the remaindermen to assess the terms of the trust, especially those that convey special privileges with regard to withdrawing corpus or those that allow the trustee to make or hold investments that tend to favor the income beneficiaries over the remaindermen.

4.2. Factors that determine present value

The entire "buyout" strategy is based upon what is a relatively straightforward concept for personal finance professionals - the time value of money or, more precisely, the present value of a dollar. The case is presented to the remaindermen in the form of two mutually exclusive options; one that can be exercised immediately and another that can be exercised only upon

the death of the trust's income beneficiary (or a successor income beneficiary, generally a spouse). In other words, each remainderman chooses between taking the present value of the future worth of its proportional share of the trust assets now or waiting for the demise of the income beneficiary and, in the case of a trust term defined by the joint lives of a married couple, a surviving spouse.

Both options, admittedly, come with "strings attached." In the case of the former, at least two major variables are open to negotiations between the income beneficiaries and the remaindermen. One bone of contention concerns the future value of the remainder interests. A realistic valuation of the remainder interests rests upon predictions of asset growth rates, asset weights within the portfolio, and the projected life expectancy of the income beneficiaries. This, of course, results in a discussion of how to determine the *rates* of growth of the various trust portfolio assets and, concomitantly, the *term* of growth of these assets.

4.3. Life expectancy

The *term* of growth means that the life expectancy of the income beneficiary or, in the case of a surviving spouse, the joint life expectancy of both must be determined. Treasury tables are generally used for this purpose, but, because they are based on averages, they do not necessarily represent the negotiators' points of view. In brief, in any given instance, the table-generated life expectancy may be, from a negotiator's standpoint, either too long or too short. A remainderman would always argue for a shorter life expectancy while an income beneficiary would vie for a longer one.

Obviously, a 50-year-old income beneficiary who is jogging or bicycling to work everyday, doesn't smoke or hang-glide, and has parents who lived into their nineties, has a strong argument that the tables greatly understate life expectancy and, thus, the life estate period. As a consequence, the present value of the remainder interest is greatly overstated (to the ultimate benefit of the remaindermen). If, on the other hand, one is representing a chain smoking "couch potato" whose parents died in their mid-fifties and who considers operating the TV remote to be regular exercise, one would not raise the issue of individual variation in longevity, but would rather keep this part of the negotiations focused on the tables.

Assuming one chooses to use the federal table rate for valuing the remainder interest to determine the present value of each remainderman's proportional share, the following wording might be an appropriate pattern for structuring the letter:

> The July 1997 federal rate for valuing remainder interests is 8%. Jack is 55 years old and his wife, Sally, is 50 years old. The remainder factor using the federal rate tables found in Alpha Volume, Table R (2)-Part 4, for two lives (55, 50) is 0.10516. This factor times 50% (your client's remainder interest) of the July 1997 fair market value of the trust ($2,000,000) is $105,160 (that is, 50% * $2,000,000 * 0.10516). This is the amount that my client is willing to pay in exchange for your client's release (or assignment) of its remainder interest. This offer is contingent upon the other 50% remainderman also accepting a similar offer.

Again, reiterating that the tables are remiss in accounting for a particular individual's health status and, thus, over or understate the value of the remainder interest, it is also important to note that they do not take into consideration special provisions in a particular trust that change the life estate from a straight life estate (or an annuity for life) to something else.

4.4. Distribution of principal

It is these specific provisions in any given trust that may persuade the remaindermen to accept a "buyout" proposal even though, initially, they are inclined to reject it. Such provisions include, but are not limited to, the distribution of principal to the income beneficiary pursuant to an "ascertainable standard" power of appointment or some other, even less restrictive, provision - for example, the trust may make corpus available if the income beneficiary wants to start a business. Under an "ascertainable standard" power, the terms of the trust give the holder of the power the right to invade the principal for reasons of "health, education, support, or maintenance." The power to invade principal under an "ascertainable standard" is found in many irrevocable trusts because the Internal Revenue Code (IRC) endorses these prerogatives as "limited powers" rather than "general powers" (IRC §2041[b][1][A]). This means that, even though the holder of such a power (for example, the income beneficiary) can benefit from its exercise, when the holder dies the trust property is not included in the estate.

It can be readily seen that the remaindermen, in choosing between the two mutually exclusive options, are faced with the time-honored conundrum of whether "a bird in the hand is worth two in the bush." Indeed, the more opportunities that exist for the income beneficiary to invade corpus, the greater the likelihood that, when the time comes, all birds will have flown and just the bush will remain. Under such circumstances, a convincing case can be made to the remaindermen for taking "a bird in the hand." They will be swayed in favor of the "buyout" option if they believe that the income beneficiaries will exercise their power to provisionally invade the corpus of the trust and/or that the costs associated with running the trust will, over time, greatly diminish its value.

4.5. Trust powers

Naturally, where there is a discretionary power to distribute trust corpus to the income beneficiaries, the extent to which the remaindermen's interest is decreased depends upon who holds this power, the degree to which the amount that can be distributed is limited either in dollar amount or by circumstance, and the probability that the discretionary power to distribute will be exercised. The authority to make distributions is usually in the form of a power of appointment. The term "power of appointment" refers to the ability of a person (the "holder" of the power) to transfer ("appoint") title to property, even though this "holder" does not necessarily own it, from the owner (generally a trustee) to someone else.

If a power is a general power, it will be included in the power holder's estate when he/she dies. By IRC definition, a general power is "a power which is exercisable in favor of the decedent [power holder], his estate, his creditors, or the creditors of his estate. . . " (IRC §2041[b][1]). All other powers are deemed to be limited powers that are not included in the holder's estate. Because of special IRC provisions, a power limited by an "ascertainable standard" and another power, called the "5 & 5" power, are two of the most common "powers" found in trusts.

A power limited by an "ascertainable standard" is, in the language of the IRC, a power that can be exercised by the holder-beneficiary only for the purpose of benefiting his/her "health,

Table 1
Negotiating weights

Provision	Power holder	Beneficiary is:	Relative decrease in remainder value	Negotiating weight
Ascertainable standard	Trustee	Wealthy	Very slight	2
Ascertainable standard	Trustee	Poor	Large	8
Ascertainable standard	Beneficiary	Wealthy	Slight	4
Ascertainable standard	Beneficiary	Poor	Large	8
5 & 5 power	Trustee	Wealthy	Slight	4
5 & 5 power	Trustee	Poor	Large	7
5 & 5 power	Beneficiary	Wealthy	Very large	10
5 & 5 power	Beneficiary	Poor	Very large	10

education, support, or maintenance" (IRC §2041[b][1][A]). This limited power can have a definite impact on the remainder interest and, thus, can be used as a bargaining chip in selling the "buyout" option to the remaindermen under certain circumstances. For instance, if the trust beneficiary has only modest income and/or the trust assets do not throw off significant cash flow for use by the beneficiary, it is much more likely that a power limited by an "ascertainable standard" will be exercised and corpus will be invaded, diminishing the amount ultimately to be received by the remaindermen.

Perhaps of greater consequence to the remaindermen (and the value they will eventually receive) is the "5 & 5" power which can be classified as either a general or limited power depending on who holds it. This power allows the power holder to distribute up to 5% or $5,000 (whichever is greater) of the trust corpus annually, on a noncumulative basis with no justification necessary. The IRC (§2041[b][2]) allows the lapse (during the holder's lifetime) of a general power to be treated as if no gift occurred provided the power that lapsed was limited to no more than the greater of $5,000 or 5% of the value of the trust. Obviously, the influence of such a power, if it exists, in promoting the "buyout" option is huge. Table 1 above is an attempt to assign numerical "negotiating weights" to the existence of each of these two powers in a trust. The higher the number in the last column (on a scale of 1–10), the greater the expected decrease in the remainder value and, consequently, the greater its negotiating weight.

The table indicates that the lowest negotiating weight goes to an "ascertainable standard" with an independent trustee and a wealthy beneficiary because it is highly unlikely that the power will be exercised. Why so? If the trustee exercises it in favor of a beneficiary who is not really in need, the trustee opens itself to being sued by the remaindermen. Compare this situation to the "5 & 5" power held by the beneficiary. It receives a 10 because it can be safely assumed that the beneficiary will definitely exercise such a power at every opportunity even if he or she is very wealthy.

5. Trust provisions that can be quantified

Some provisions in a trust, such as a 5 & 5 power held by an income beneficiary, can be valued because it is correct to assume that the beneficiary will exercise this right of

withdrawal each and every year, and at the earliest opportunity. Likewise, one can assume that withdrawal will occur if a provision permitting a specific sum to be withdrawn for a particular purpose (for example, up to $100,000 for a down payment on a home) exists. Even if the withdrawal must be delayed, its present value can be determined.

Other provisions, such as trustee fees and the cost of accountants to prepare trust income tax returns, can generally be quantified with some degree of accuracy. The trustee fees are usually some small percentage of the trust's value (for example, 1% of year-end corpus value) and the cost of tax return preparation is an annually occurring expense that can easily be valued.

6. Trust provisions that cannot be quantified and their effect on valuation

Provisions that cannot be precisely valued are those that allow considerable discretion as to the amount and timing of distributions of corpus. Included in this category are powers held by an independent trustee where the beneficiary's needs must be taken into account. Such powers might be those limited by an ascertainable standard. For example, if the income beneficiary is in need of extra money immediately, will this be true in the future? Or, if wealthy now, will he or she be able to maintain that level of wealth? Obviously, the beneficiary's immediate circumstances will be given some weight, but how much is open to argument. Needless to say, the poorer the income beneficiary, the stronger the case for distributions of corpus and the lower the value of the remainder interest. Naturally, the reverse is true if the income beneficiary is wealthy or if the trust itself is so large that the income throw-off by itself will make the beneficiary affluent.

Other provisions whose impact on the remainder interest cannot be precisely measured include:

Circumstances relating to the income beneficiary such as

- His or her health
- Whether he or she has medical insurance
- His or her lifestyle (For example, is he or she a smoker or nonsmoker, a nondrinker, a social drinker, or a problem drinker?)

Matters relating to the trust such as

- The relationship between the trustee and the income beneficiary
- Whether there is a provision specifying that the income beneficiary's interest takes preference over that of the remaindermen
- The restrictions in the trust regarding the types of investments that can be made by the trustee (State laws generally favor diversified portfolios for trusts. The Uniform Probate Investor Act adopted by many states makes trust asset diversification the general rule, e.g., CA Probate Code §16048: "In making and implementing investment decisions, the trustee has a duty to diversify the investments of the trust unless, under the circumstances, it is prudent not to do so." However a restrictive clause in a trust

would have to be followed unless the trustee obtained court approval to invest differently.)
- The extent to which the trust incurs transaction costs, including commissions, capital gains taxes, and investment advisory fees

The circumstances of the remaindermen such as

- The possibility of adverse publicity if a "deal" *is* struck or being deemed heartless if one *is not* struck
- One or more of the remaindermen being a minor (Here, court approval of a "buyout" may be required. And a court may require the appointment of an attorney to represent the "best interest" of the minor. His or her understanding of present value concepts and the ensuing benefits of such an arrangement may be lacking.)

7. Valuation: a complex example based on an actual case

The following hypothetical example is based on an actual case. The successfully concluded negotiations took place several years ago. This example is used to present the numbers and to suggest language for a written approach to the remaindermen with likely responses and appropriate counter responses included.

The settlor (grantor) established a living trust, retaining all interests until his death. Upon his death, the trust became irrevocable. The settlor's 54-year-old son was given a life estate in the trust, with his 48-year-old spouse (the settlor's daughter-in-law) receiving a following life estate in the event she outlived him. The trust did not condition her contingent income interest on her being still married to the son at his death (that is, she would have the income interest simply by outliving him). Two highly regarded universities, a charity involved in the law, and an adult grandson were named as the remaindermen, each to receive a 25% share.

When the settlor died the trust corpus was worth approximately $1,390,000 after all death taxes had been paid. The trust terms allowed the trustee to invade corpus for the benefit of the income beneficiary based upon an ascertainable standard related to "health, education, support, or maintenance." Another provision stated that the interests of the income beneficiaries were to be considered before those of the remaindermen. And, yet another, allowed the trustee to distribute corpus so as to allow the income beneficiaries to start a business. These provisions that favored the income beneficiaries, and the fact that the beneficiaries were given all income rather than a fixed dollar or fixed percentage amount, kept the trust from qualifying for a charitable estate tax deduction (see IRC §2055). In addition to this favorable treatment, both income beneficiaries were in very good health.

In implementing the remaindermen "buyout" offer, several steps were crucial. First, a determination of the appropriate growth rates was made for the different components of the initial trust portfolio. Historical rates of capital appreciation were gathered from *Stocks, Bonds, Bills, and Inflation 1995 Yearbook* (Ibbotson Associates, 1995, Chicago, IL).

Second, a weighted average was used to determine the growth of the portfolio as a whole. Table 2 portrays the expected portfolio growth.

Third, this expected growth rate was projected out for a 38-year joint life expectancy

Table 2
Expected portfolio growth

Investment	% of Corpus	Expected cap. appr. per year	Weighted cap. appr.
Bonds	50%	0.0%	0.00%
Stocks, large cap	30%	5.4%	1.62%
Stocks, small cap	10%	12.5%	1.25%
Foreign stocks (22 year history)	10%	9.7%	0.97%
Expected ann. portfolio appr.			**3.84%**

starting with the portfolio value of the trust as of March 31, 1995. This projection took into account the capital gains tax (combined federal and state of 29%, which one might want to reduce to 22%, or even less, in light of the 1997 tax act's capital gains rate reduction) on a 20% annual turnover of the portfolio, transaction costs of 0.5%, and annual trustee's fees charged to corpus of 0.5% of the value of the corpus.

Fourth, the present value of the trust at the end of the 38 years was calculated using 9.2% discount rate, which was the average IRC Section 7520 rate for the months just preceding the negotiations. Based on the example data just presented, the present value for the trust remainder interest was $83,177. Therefore, each 25% share was worth $20,794, which was rounded up to $21,000 as an initial offer.

It is worth mentioning that copies of schedules showing the growth of trust assets (taking into account taxes, transaction costs, and trustee fees) were attached to the letters to the remaindermen. In addition, the letters set forth the calculation of the valuation of the income and the remainder interest, as well as the assumptions underlying those calculations. Moreover, it should be recognized that the determination of an appropriate discount rate might be a sticking point. While IRC Section 7520 directs the Treasury to provide rates for valuing income and remainder interests on a monthly basis, income beneficiaries would naturally argue for a higher rate while the remaindermen would advocate a lower one. In this particular case both parties used the 9.2% discount rate for their calculations.

Fifth, an argument was then made that, given the power to withdraw corpus to start a business and the excellent health of the income beneficiaries, the use of the Treasury table factors greatly overstated the remainder values. (At the same time, the income beneficiaries fully realized that making an offer that was ridiculously low would create an environment in which it would not be worth the remaindermen's trouble to negotiate a settlement). Furthermore, it was pointed out that some of the assumptions regarding costs were conservative, resulting in a higher value of the remainder interest than actual practice might justify.

> The assumption of a 20% turnover per year in the portfolio is very conservative as studies of mutual funds show that turnover rates generally exceed 50% per year, and increased turnover rates accelerate the recognition of capital gains and increase transaction costs, both of which act as a break on capital growth.

Finally, since this was a private inter vivos trust, the income beneficiaries chose not to disclose to the charitable remaindermen each other's identity until all four remaindermen

were in agreement, at least in principle, to negotiate a transfer of (sell) their remainder interests. The wording in the letter to the remaindermen was along these lines:

> This letter is to open discussion; it is not an offer that can be immediately accepted since my clients wish to retain the option to go forward only if settlement can be reached with all four remaindermen. From our initial conversations, it looks like this can be accomplished. Once all four of you have indicated an interest in selling your remainder interest, you will be given the names of the other remaindermen. It is my clients' intent that each remainderman receive the same payment, one that represents a realistic payment of the value of the interest that you each give up.
>
> We believe the offer is exceedingly fair for a number of reasons: the tables greatly overstate the remainder value, given the ease with which the income beneficiaries can remove the corpus from the trust; since the trust terms express a preference for the income beneficiaries, the trustee has the option of increasing income at the expense of growth; the joint life tables understate my clients' joint life expectancy given that neither of them smoke, both exercise, both enjoy good health and both have excellent medical benefit packages through their employment; and the assumption of a 20% turnover per year in the portfolio is very conservative as studies of mutual funds show that turnover rates generally exceed 50% per year, and increased turnover rates accelerate the recognition of capital gains and increase transaction costs, both of which act as a break on capital growth.

Once all the remaindermen indicated their willingness to sell and the asking prices were within a range acceptable to the income beneficiaries, the charitable remaindermen were put in touch with one another. The income beneficiaries' son (the settlor's grandson who was appropriately represented by independent counsel) agreed early in the negotiations to take whatever share the three charitable remaindermen took. The charities' initial counter offers (in response to the $21,000 "buyout" offer) were respectively: $29,000, $30,000, and $41,000. Just the latter seemed out of line on the high side.

Interestingly, the charitable remaindermen actually ignored the income beneficiaries' power to withdraw corpus to start a business and its depressing effect on the value of their remainder interests. Apparently, this would have dropped the remainder value so low that further negotiating would have been pointless and the "wait and see" option would have been adopted instead. Consequently, the income beneficiaries decided not to push this issue and its associated lowering effect on the remainder value. After conferring with one another, the charities offered $30,000 per interest and accepted a counter offer of $25,500 per interest. The trust was liquidated in August of 1995. At the time of its liquidation the trust's value had risen to approximately $1,500,000. Hence, after the payment of $102,000 to the remaindermen (and compensating the trustee and the attorney), the income beneficiaries received, free of trust, an amount just slightly in excess of $1,390,000.

Not only were the income beneficiaries happy with the result, the Director of Planned Giving at one of the charities wrote a thank you letter stating:

> On behalf of all of us at [the university], I want to thank you, [the income beneficiaries], and [the trustee] for your help in making the [settlors] Trust gift to [the university] possible. In the many years that I have been involved at [the university], this gift was unique. Needless to say, we are pleased and grateful to [the settlors] for their thoughtful vision and interest.

> Please will you convey our gratitude to your clients. . . . Again, I thank you for your assistance in this matter and send best regards from [the university].

Clearly, he understood the present value concept.

8. Situations where liquidation is inappropriate

Quite obviously, there are instances in which liquidating a trust would be an unfortunate strategy. For example, where the income beneficiaries are incapable of wisely handling an outright inheritance, tying up the property in a trust may be in the best interests of all persons concerned. Even if the settlor's children are quite capable of handling the property, the settlor may still prefer to restrict their interest to that of a life estate. (This may be particularly true if there are no grandchildren and none are likely.) In short, the settlor may like the idea that *he* or *she,* and not the children, has purposefully chosen the ultimate owners of the property (the remaindermen). This desire might be particularly strong if the remaindermen are the settlor's favorite charities. Of course, liquidation of the trust would be a moot point if the settlor placed a clause in it that prevented the remaindermen from selling their interests. (For example, "Any attempt by a remainderman to sell its interest shall cause that remainderman's interest to terminate, and said interest shall instead go to charity 'X.' ")

The income beneficiaries might be well advised not to pursue a "buyout" strategy if they are having personal financial problems and/or are faced with possible lawsuits. A life estate, especially if the trust contains a "spendthrift provision," is less attractive to creditors than property owned outright by debtor.

A remainderman may be quite loathe to sell its remainder interest if "bad press" might result from the disclosure that a one million dollar gift in the future was "traded away" for a mere fraction of said value today. Of course, this gross misinterpretation is a realistic concern due only to the general public's lack of understanding of the time value of money and/or public relations difficulties that some charities have had in the recent past. Unfortunately, charities may be concerned that potential donors may hear about such settlements and, fearing that their "generous" gifts may eventually be whittled down to something that seems quite paltry, decide to give it to some other charity. After all, with a future $2,000,000 gift a library might well bear the donor's name, whereas today's $100,000 gift might result in the name appearing on a long list of donors on some recognition plaque in the reference section.

9. Conclusion

This paper has attempted to describe verbally, and through example, an approach to liquidating a life estate in situations where the income beneficiaries are competent to handle the corpus of the trust and to establish that this can be done to the shared benefit of both the income beneficiaries and the remaindermen. This simplification in personal finance involves employing a portion of the trust assets to "buyout" the interests of the remaindermen. The

consequence is a termination of the trust, leaving the income beneficiaries to manage the remaining assets, without the costs and impediments associated with a trust, and the remaindermen with immediate cash to spend or invest as they see fit.

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