ANALYSIS OF CRUMNEY AND CLIFORD TRUSTS
AND CROWN LOAN IN FARM ESTATE PLANNING

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RECOGNITION

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ANALYSIS OF CRUMMEY AND CLIFFORD TRUSTS
AND CROWN LOAN IN FARM ESTATE PLANNING

Introduction

Traditional farm estate planning concepts have been greatly altered by new tax laws and, therefore, consideration of professional advice and management has become necessary. Good estate planning is much more than just saving taxes. Personal goals - making sure the right people get the right assets, children's educational needs, helping one or more children continue the family farm, and providing financial security for the survivors - are even more important to most people than saving taxes.

Our present inflationary economy is rendering it difficult for the family farm and family to survive. Today's farm families must use all resources available to them to provide for their financial objectives.

The estate and financial planning instruments considered in this analysis are the Crummey Trust, Clifford Trust, and the Crown Loan. A questionnaire was used to compare the efficiency of these three devices.

Methodology of Questionnaire

The objective of this questionnaire was to determine if the CPAs as a group chose one alternative or method over another as compared to attorneys as a group. Other comparisons of the results were tabulated using the information gathered. The issue of trust versus loan is questioned. It also stresses the intended financial strategies of the couple in the Farm Estate Example. They hoped to minimize taxes, provide resources for their children's college educations and to maintain adequate retirement funds for themselves.

The survey population included Indiana CPAs and attorneys. A random sample numbering one hundred was chosen from each group. The CPA names were taken from The Public Accountancy- Register of Certified Public
Accountants, May 16, 1983 edition. The practicing attorney participants were retrieved from the Martindale Hubbell Law Directory - Volume III.

The questionnaire itself was fourteen questions in length. Five of these covered various demographic topics: profession, years in practice, clients' occupations, and experience in farm estate planning. A farm estate situation is given and the remaining questions ask for advice concerning the three alternatives to solve the couple's objectives. A copy of the questionnaire is in the Appendix - Exhibit 1.

The questionnaires were first mailed out with an explanatory cover letter in December, 1983. A second followup letter was also sent in February, 1984, to those participants who had not yet responded. The results of the completed surveys were then compiled and statistical tests were completed through the computer. The results will be listed and analyzed in a later section.

A total of seventy questionnaires were returned but only 39 were applicable to the research. Cut of the 31 not completed, 13 were attorneys, and 18 were CPAs. The reasons given for the incompleteness were time constraints, working in private accounting rather than public accounting. The majority of those expressed a lack of experience in the estate planning field and they did not feel qualified to answer the questionnaire.

The next section deals with the three estate planning techniques chosen for this example. For each of the trusts and loan, general background information, requirements and disadvantages and advantages are listed.

Estate Planning Devices

Crummey Trust

The Crummey Trust is an irrevocable trust which is funded by cash or other property. It has been used in situations where individuals
wish to make gifts for the benefit of their children or others. This instrument enables the donor to both restrict the use of the funds by the donee and to obtain the $10,000 present interest gift tax exclusion (before 1982 the gift tax exclusion was $3000). This type of trust usually allows that a maximum amount (usually the lesser of the amount contributed to the trust during the year or a stated dollar amount) can be withdrawn by the donee up to the end of the calendar year. Any amounts that are not withdrawn are held in the trust for the extended period until the final distribution to the donees.¹

The Crummey Trusts were based on the holding in the 1968 Ninth Circuit decision in Crummey v. Commissioner. In this case, the grantors, a husband and wife, established four irrevocable trusts for their four children, three of whom were minors. These trusts provided that any individual could add to the trust principal. Each beneficiary was also given the right to demand distribution of up to $4000 not later than December 31 of the year in which the additions were made. If the beneficiary was a minor, then the distribution right was passed to the minor's guardian. Under this form of trust an independent trustee may, in his complete discretion, distribute or accumulate income for this minor child. When the trustee feels a reasonable "emergency" and/or educational cost has arisen, then the trustee may invade the trust principal for the benefit of the child.²

The question the Court considered was whether a present interest includes the right that a minor child has to make a demand for the distribution of the corpus added to the trust even though no guardian had been appointed as of the date of the gift. The Court held that just because a guardian had not as yet been appointed did not prevent the creation of the present interest.
The concept of present interest versus future interest is explained in the following example. If a spouse and the children derive no benefit from a trust until the death of the grantor, which is the case if the trust owns only life insurance, then the gift is considered to be a gift of a future interest. A gift of a future interest could also result even when life insurance policies are not involved. So if the trust income is accumulated and distribution of principal is deferred this would be considered a future interest. The problem is that the annual exclusion is available only for the gift of a present interest. The Crummey Trust provides a solution to this problem through the right to withdraw on the part of the beneficiary. This makes the gift one of a present interest. 3

The consequence of the Crummey decision has allowed a donor-parent to effectively prevent a beneficiary from possessing or obtaining enjoyment of trust property during the period that the beneficiary is still a minor. The parents are usually the source of additions to the trust which eventually passes to the beneficiary. The donor also is able to discourage a beneficiary from making Crummey withdrawals after the beneficiary reaches majority. The IRS has accepted the Court's holding in the Crummey case but it has ruled that an adult donee must have knowledge of his right to withdraw and a reasonable time (defined as at least a month) to make such a withdrawal. 4

Crummey Trusts usually have the following characteristics. The grantor creates an irrevocable intervivos (living) trust. The trust does not contain any prohibited powers or assets that would cause the trust to be taxed to the estate at grantor's death.

A common trust principal is a life insurance policy. The trustee is empowered to borrow against the cash value of the policy. Any income produced is used to pay the life insurance premiums on the policies owned by the trust. There is usually not enough income generated to pay
the full amount of the premiums. To provide for the remaining premiums, the grantor makes periodic contributions to the trustee, who uses these funds to pay the premiums on the trust policies. These are not considered as future interest gifts because the trust provides that each beneficiary has current right to withdraw his share of the trust contribution. Thus, the donor can take advantage of the annual gift tax exclusion.

At the death of the insured grantor, the proceeds of the insurance policies would flow into the trust to be invested and distributed by the trustee in accordance with the trust terms. The grantor must live for more than three years after the transfer of the policies for them not to be taxed in his estate at death.

The unique characteristic of Crummey Trusts is the withdrawal rights given to the trust beneficiaries. The donee of the right can immediately demand withdrawal of contributions to the trust, no matter what form these contributions take (cash, policies, etc.). The donee is made aware of this right and is advised of each contribution within a reasonable period of time. The donee is then given a reasonable time in which to make demand before the right to withdraw lapses. This right is noncumulative. If the donee does not exercise the right to withdraw, the contribution is irrevocably added to the trust principal. The trust instrument provides that the beneficiary, his natural guardian or a legally appointed guardian of the beneficiary can receive notice and exercise the withdrawal right.

The withdrawal right arises only when a transfer is made to the trust. It becomes effective only when it is necessary to qualify the contribution to the trust as a present interest gift. The right of withdrawal is limited in scope to those assets transferred to the trust currently and extends only to the value of assets equal to the donor’s available gift tax exclusion.

Ordinarily, all trust income, credits and deductions are taxed to
the trust itself and/or to its beneficiaries, depending on the specific trust terms. The provisions of the trust instrument should indicate whether the trust or its beneficiaries will bear the tax burden or derive the benefit of excess deductions. When the grantor holds certain powers, he will be taxed on the trust income. Credits and deductions will be passed to the grantor also.

The discretion to use trust income to pay life insurance premiums on the life of the grantor should not result in the trust being included in the grantor's estate. However, if the grantor had the unrestricted power to remove or discharge a trustee at any time and appoint himself trustee, the grantor is considered as having the power of the trustee and the trust will be includible in the grantor's estate. 6

The scope limitation provides a method for computing the portion of trust deemed to be owned by a donee. To compute the portion of trust income attributed a donee, use a fraction. The numerator should be the amount subject to owner's control and the denominator should be the fair market value of the entire trust corpus at the beginning of the tax year. The time limitation has considerations also. For example, if a donee's withdrawal right begins October 1 and ends December 31 then the fraction 1/4 would also be used in the calculations. So if the grantor wants the income to flow to the beneficiaries and be taxed at their rates, then the withdrawal rights should be structured to last the entire year. 7

There are some risks in using the Crummey Trust. The Economic Recovery Tax Act of 1981 brought about one of these complexities. The increase of the annual exclusion from $3000 to $10,000 per year resulted in a lapse of the Crummey demand power. If the lapse is a "transfer", the former power holder has created a grantor trust with its consequent income liability. The release of a general power of appointment is considered a transfer of power by the individual possessing such power. If
the beneficiary fails to exercise the power to withdraw property, the beneficiary may have made a gift of the property to the remaindermen of the trust. This is because the beneficiary became the owner of the property under the power of appointment rules, and persons other than himself, the remaindermen, will benefit from the lapse. The gift to the remaindermen will not qualify for the annual exclusion because the gift is a gift of a future interest. An exception under the Crummey Trust rules is often called the Five and Five Power. If the power to withdraw is limited to the greater of $5000 or 5% of the trust corpus, the lapse of power is not considered to be a gift by the beneficiary.8

Prior to January 1, 1982 many users of the Crummey Trust usually allowed for annual withdrawals of $6000 maximum so that the donor could claim the maximum amount of interest exclusion where gift-splitting was elected. Even if a problem with the lapsed power of appointment arose, it was probably ignored because this gift was not noticed or the value of claiming the exclusion was worth the "risk" of having a portion ($1000) of the trust subsequently included in the donee's estate.9 Today estate planners must consider these limits more closely.

During the period in which a Crummey power of withdrawal is outstanding, the Code treats the beneficiary as owner and is taxed on that portion of the trust that the beneficiary has the power to withdraw. The beneficiary will be required to report these items of income, deduction, and credit on this trust portion. This occurs whether or not the trustee exercises his discretion to make a current distribution.

Additional risks that have become more apparent now since 1982 include:

1. The lapse to the extent it exceeds $5000 or 5% of the trust principal will be treated as a gift by the donee of part or all of the amount foregone unless donee is both the income and remainder beneficiary. If the
donee has made a taxable gift, the tax consequences are:
(a) the gift may be a future interest.
(b) there will be a payment of tax and/or utilization of the unified credit, and
(c) there will be an addback of adjusted taxable gifts upon the donee's death.

2. Where the donee is not an income and/or remainder beneficiary and, during the life of the trust has or will have certain rights in the trusts, the failure to exercise the power to withdraw in each year it exists results in a lapsed power of appointment to the extent that this lapsed power exceeds the greater of $5,000 or 5% of the value of the corpus.\[^{10}\]

A portion of the trust's fair market value at the date of the donee's death will be included in the estate if the donee dies before the trust actually distributes its principal, even though the property goes directly to whoever the instrument directs if the original donee dies.

For example, assume that a donee can withdraw up to $20,000 of the property contributed each year and will receive the income off of the trust. The donor contributes $20,000 in year 1 and $20,000 in year 2 to the trust and there has been no appreciation in the value of the assets. No further contributions are made. If the donee dies before the trust terminates, there will be included in his estate 25% of the fair market value of the entire trust, including any appreciation (15,000/20,000 for year 1 plus 15,000/40,000 for year 2 - the amount of the lapse in excess of the greater of $5,000 or 5% divided by the fair market value of the trust at the time of the lapse). This occurs even though the donee did not receive any of the property or have the ability to decide to whom it passed.\[^{11}\]

Many donors do not wish to transfer the total income or trust principal to the children when they reach twenty-one. They frequently want
to delay this transfer until the beneficiaries reach the age twenty-five or thirty or even later. The Crummey Trust is a planning tool which assures the existence of a "present interest", while at the same time providing the donor with a mechanism for deferring indefinitely the beneficiary's possession and enjoyment of the trust corpus and/or income. The $15,000 differential between the post 1981 ERTA $20,000 split-gift annual exclusion and the $5000 limitation that now would be lost is substantial. This is likely to have quite an impact on future gifts to minors. Some non-tax advantages of the Crummey Trust are that it provides investment management and allows for more equal treatment of children (such as one child just approaching college and another has already received a college education).

**Clifford Trust**

This relatively simple and effective tax-cutting device is an irrevocable short-term trust that must be created during the lifetime of the grantor. The Clifford Trust originated through a 1940 Supreme Court Case. George B. Clifford, Jr. drew up a five year trust for his wife and appointed himself trustee. He claimed the earnings were his wife's and should be taxed at her lower rate. The IRS and Supreme Court disagreed. They stated that five years was too short of a term for a legitimate trust. In 1954 regulations were passed that allowed the grantors to escape taxation on trust income if the trust lasts for at least ten years and a day and the grantor has no power over the trust during this period. The Court felt that the combination of a short duration of the trust, retention of control by the grantor, family relationship, and his wife's benefits, all gave George Clifford, Jr. the same equivalence in ownership as he had before the trust was established.
The issue is essentially the recognition of the trust as a separate, viable entity apart from the grantor. If the trust fails this, the grantor is treated as the owner of the corpus and the grantor receives the income and is entitled to the deductions. The term length of ten years is a minimum number of years for the trust to be in existence. If one wishes to establish the trust for a longer period of time, this may be done without any problem. However, the entire amount to be placed in a trust must be done at one time because each time any additions are made to the trust this is equal to the creation of a new short-term trust. These additions in turn must meet the ten year requirement in order to receive the favorable income tax benefits.\textsuperscript{14}

As mentioned earlier, the Clifford Trust must last more than ten years or the lifetime of the grantor (provided he has an actuarial life expectancy of more than ten years) or the lifetime of the beneficiary (regardless of how long the beneficiary is expected to live). During the trust term, the income from the trust principal can be passed through and is taxed to the named beneficiaries. At the end of the trust term the principal assets revert back to the grantor.\textsuperscript{15} Thus the main purpose of a short-term trust is to shift the income produced by the trust assets to the beneficiaries. An appointed trustee will pay out this income to the named beneficiaries who should be in a lower tax bracket and have an immediate need for these funds.

With the reductions in government funds for student loans and aid, many parents have found the need to look for other ways to assist their children for college expenses. Usually the parent puts a smaller amount into a trust some years before the child would begin college. The trust income is either retained for the child to use during college or is periodically distributed to the beneficiary. To abide by the ten year
restriction, the Clifford Trust could be set up six years before the child would begin college.

Some various tax consequences of the Clifford Trust follow. Undistributed income is taxed to the trust and distributed income is taxed to the beneficiary. The grantor cannot use the income of the trust to support someone whom the law says the grantor is legally obligated to support anyway (wife, minor child, and in some states, indigent parents). If the grantor does, then the income of the trust is taxed to the grantor to the extent it is used for support. In some states, parents are obligated to pay for their children's education so the income of the short-term trust would be taxed to the parent. This varies from state to state and it depends on the family's standard of living.

There are also some estate taxes on the short-term trust principal. The value of the grantor's reversionary interest (the right to get the trust principal back) is included in his estate. At the time the trust is created, the value of the reversionary interest is about 56% and this value increases as the termination date draws nearer. For example, if the trust term only has five more years, about 75% of the trust principal would be included in his estate and taxed. This assumes the trust does not end upon grantor's death and the grantor has not assigned the reversionary interest to someone else. There is double taxation on the trust principal if, after it reverts back to the parent, the grantor (parent) dies. The portion taxed is the excess over the annual gift tax exclusion and unified credit.\[16\] Every person has a unified tax credit. It can be used to offset the tax on gifts made during life or to reduce or eliminate the federal estate tax at death. The Unified Credit Schedule that follows provides the necessary information. The third column shows the maximum amount of taxable estate the credit will offset.
<table>
<thead>
<tr>
<th>Year of Gift or Death</th>
<th>Unified Credit</th>
<th>Credits Offset Tax on this Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1981</td>
<td>$47,000</td>
<td>$175,625</td>
</tr>
<tr>
<td>1982</td>
<td>62,800</td>
<td>225,000</td>
</tr>
<tr>
<td>1983</td>
<td>79,300</td>
<td>275,000</td>
</tr>
<tr>
<td>1984</td>
<td>96,300</td>
<td>325,000</td>
</tr>
<tr>
<td>1985</td>
<td>121,800</td>
<td>400,000</td>
</tr>
<tr>
<td>1986</td>
<td>155,800</td>
<td>500,000</td>
</tr>
<tr>
<td>1987</td>
<td>192,800</td>
<td>600,000</td>
</tr>
</tbody>
</table>

The primary problem with the short-term trust is the gift tax on the value of the income that has been shifted to the trust. Real estate is a good asset to place in a short-term trust but it should have high income production so that the income tax savings can be realized. It should be free of debt so that the income is not reduced by interest payments. It is also advisable to have a non-family member as trustee.

Another factor that might affect the decision to use a short-term trust is the rule that capital gains on principal during trust term are taxed to the grantor. The theory behind this policy is that since the property reverts back to the grantor after the trust terminates, the grantor should pay tax on the realized appreciation. This additional tax can be avoided by stating in the trust instrument that such capital gains will be distributed and taxed to the beneficiaries either when realized or when the trust term ends.

Some individuals are reluctant to establish a Clifford Trust because of the time constraints and irrevocability of the trust. The prospective grantor must decide whether the grantor can afford to lose the use of the corpus for ten year plus period and income transferred to the trust. A transfer to a trust followed by a loan-back or lease-back of the property to the grantor may be a possible solution.

The advantages of this technique are most beneficial to high bracket grantors without substantial liquid assets. The best means of providing for the initial funding of the trust, and the length of time...
between the gift to the trust and the loan-back, depends on a number of things. If the trust is not able to earn an amount equal to the interest rate paid by the grantor, then it is best to make the loan-back as soon as possible.18

This variation of the standard Clifford Trust can be useful in small business or farm operation. A grantor can give property used in the trade or business to a Clifford Trust and then lease the property back, and the rent paid on the lease to the trust is deductible. Several criteria must be followed:

* The grantor must not retain substantially the same control over the property that he had before he made the gift;

* The leaseback should be in writing and must require payment of reasonable rent;

* The leaseback (as distinguished from the gift) must have a bona fide business purpose;

* The grantor must not possess a "disqualifying equity" in the property. The courts have held in past cases that retaining a reversionary interest does not result in a "disqualifying equity" interest in the property.19

The IRS has attacked some gift-leaseback arrangements in the past so these must be carefully planned and properly documented.20

December 1, 1983 the Internal Revenue Service made the Clifford Trust a less appealing tool for educational aid and tax savings. Formerly the parent could give a child as much as $10,000 a year (20,000 from a couple) without having to pay federal gift tax. Because the money loses its value over the period of the trust, the IRS has allowed the initial investment into the trust to be as much as $45,290 before the grantors owed any gift tax.

On December 1, the IRS revised the actuarial tables so a couple starting a trust after this date would be able to set aside only
$32,549 before gift tax was due, a 28% cut in the contribution limit. This increase resulted from the change in the yields on treasury bonds. 21

In situations where parents use income-producing property (stocks, real estate, savings, etc.) to provide funds for college expenses or support for parents, the Clifford Trust is a viable alternative. To give the student or parent the income to be taxed at a lower rate, the grantor has to give the beneficiary the asset that produces the income. These assets are not given away forever. Eventually the grantor gets the property back. 22

Crown Loan

An interest-free loan has been named a Crown Loan. This technique got its title from the 1978 Crown decision in which the issue was whether interest foregone on a loan constituted a gift. Crown and his two brothers had loaned $18 million through their partnership to a series of twenty-four trusts set up for the benefit of their children and other close relatives. The Seventh Circuit agreed with the Tax Court's decision that the partnership's failure to charge interest on the loans was not a transfer subject to a gift tax. However, in 1982, the Eleventh Circuit ruled that interest-free demand notes are subject to gift tax so this aspect of interest-free demand loans is once again unsettled. 23

A summary of the situation in question is as follows: the taxpayer (D) made substantial interest-free loans to his son (L) and to Corporation A, owned by D, L, their wives, and L's sons. All but two of the loans were demand loans. When the IRS surveyed the situation it determined that D's loans resulted in taxable gifts in the value of the use of the money lent. Seventh Circuit Tax Court ruled against this but the Court of Appeals reversed the decision, holding that interest-free
loans, whether for a fixed term or on a demand basis, are subject to the gift tax. In a more recent revenue ruling, parents loaned their child $50,000 in exchange for a promissory note. The parents then borrowed the money from the child, giving a mortgage on their home as security. The parents deducted interest payments made to the child and the child reported the interest income. The "interest payments" were about equivalent to the yearly college tuition costs of their child. The IRS concluded that the only purpose of the transaction was to enable the parents to deduct the cost of their child's education as an interest deduction. Thus, the parent's interest deduction was not allowed but the child did not have to report the interest income.

An interest-free demand loan has several advantages over short-term trusts. The legal costs and administration fees are much less and there is usually a reduction in paperwork since making a loan does not require a formal trust document or trustee. The lender does not have to part with the income-producing property for ten years and one day. Since the child can repay the loan at any time, the parent can regain the use of the money in less than ten years. Only the principal of an interest-free loan is subject to estate tax whereas in a short-term trust, the transfer may be subject to a gift tax at the time of the transfer. The interest-free loan also has benefits over trusts when substantial cash is available. The income from this cash invested in interest-bearing obligations is taxed at the very highest rate on the individual income tax rate schedule. Currently, interest income does not qualify for the maximum tax on earned income and it does not qualify for the capital gains tax. Loaning this money to children or individuals in lower tax brackets is one of the most effective methods
available for shifting this income.\textsuperscript{27}

Once again control of the funds is a factor in who is responsible for the taxes. If the loan is to an adult child and the parent has no control over the funds, the child will be taxed on the earnings. However, if the parent still has direct or indirect control over the funds, the IRS has grounds to claim no loan was actually made and thus the parents are taxed on the income. In most states, if the child is a minor (18 or 21) when the loan is made, then it is possible the loan is not enforceable and parents are taxed. This clause should be investigated before making any loans for college.

When the child is an adult and the parent has no control over the fund, the child determines the use of the money. However, if the child pays more than half of self-support, the parent may lose the dependency exemption. The amount loaned must be large enough to produce enough current income to pay the taxes and yet leave enough for the intended purpose.

If the lender dies before collecting on the loan, the principal is included in the estate as a loan receivable. There are no reversionary interests so no double taxation problems arise.\textsuperscript{28}

The loan must be intended to be repaid. However, the parent must give up complete control of the funds to receive the tax benefits so absolute return of the principal is uncertain. Some non-tax considerations come into play. Will the child use the money for the intended purpose? Will the child repay the loan? It depends on the integrity and financial ability of their children. The loan must be a demand loan with no repayment terms. If repayment terms are specified, interest will be imputed at the going rate for similar notes with similar security, and treated as a gift.\textsuperscript{29}
As long as the lenders do not lend more than what would result in greater interest than the $10,000 or $20,000 gift tax exclusion they do not have to worry about this tax consequence. For example, a married couple can loan at least $100,000 to each child interest-free (assuming an interest rate of 20% or less) since the "foregone" interest on the $100,000 would be less than the $20,000 annual gift tax exclusion allowed. This should be more than enough to generate sufficient income to provide funds for college expenses.

One reason that a substantial amount of cash must be available at the start is that a parent usually loans a large lump sum to a child which is then invested to generate the money for current educational expenses. After the child finishes college, the loan is to be repaid. Whereas with a short-term trust a relatively small amount is initially invested and is allowed to accumulate over the years.

Corporations can also make interest-free loans to shareholders or employees. Farms that incorporate can use this device to accomplish some tax planning objectives. To the skilled and informed accountant or lawyer, the interest-free demand loan can provide a wide range of timing and income shifting opportunities but they must be aware that the IRS has become much more aggressive in its monitoring of this planning tool. In 1961, the Tax Court handled a case concerning an interest-free loan from a closely-held corporation to its shareholders. The Tax Court held this did not result in taxable income to the loan recipient. The question is whether this is dividend income or a bona fide loan. In the corporate case much more documentation is required. A corporate resolution would state that the corporation has considered and approved the loan, conveyed the underlying business purpose of the loan and terms of the loan, including repayment and the security provided by the
borrower. The promissory note should be dated, signed by all parties involved, indicate that it is interest-free, and state a maturity date unless it is a demand loan and contain a repayment schedule. 30

The main advantage of the interest-free Crown Loan is its overall simplicity as compared to the other trusts but it has its risks. With competent advisers, parents can make some wise moves but they should weigh the advantages of trusts and loans.

Questionnaire Results

Out of the 200 questionnaires mailed out 39 completed forms were returned. This is a 19.5% response rate. There were 18 CPA, 17 Attorney, and 4 Both (individual was both a CPA and Attorney).

The response group as a whole had a varied background in their field as illustrated by the following chart.

Survey Population Experience

[Graph showing distribution of years in practice]

Their practices included serving clients with diversified occupations. Unfortunately a substantial percentage of their work was not for agricultural clients. The CPAs had 12.8% of their clients in farming as compared to 25.6% of attorney's clients. For over 75% of the CPAs and attorneys less than 20% of their clients seek estate planning advice.
The percentages show both groups doing an average of 15% in estate planning. Out of the estate planning that is done the following is the breakdown pertaining to farms:

<table>
<thead>
<tr>
<th>Farm Estate Planning Experience</th>
</tr>
</thead>
<tbody>
<tr>
<td>% of Farm Estate Planning</td>
</tr>
<tr>
<td>---------------------------------</td>
</tr>
<tr>
<td>0%</td>
</tr>
<tr>
<td>Less than 10%</td>
</tr>
<tr>
<td>10% to 20%</td>
</tr>
<tr>
<td>Over 20%</td>
</tr>
</tbody>
</table>

One difference between the response group is the category - Years in Practice. The attorneys had more years of experience than the CPAs. None of the attorney respondents had less than five years and 47% had over twenty years in practice. The CPAs averaged 5 - 10 years of experience. The older respondents (over 10 years in practice) also had more estate planning business. The over 20 year group had significantly more farm estate planning clients.

In regard to providing for the Carlsons' children's college educations, the percentages were as follows:

<table>
<thead>
<tr>
<th>Estate Planning Device : College Education</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crummey Trust</td>
</tr>
<tr>
<td>CPA 5.8%</td>
</tr>
<tr>
<td>Attorney 7.7%</td>
</tr>
<tr>
<td>Both 25.0%</td>
</tr>
<tr>
<td>TOTAL 8.8%</td>
</tr>
</tbody>
</table>

Both the attorneys and CPAs felt that more than one of the given
factors (See Appendix - Exhibit 1 - Questionnaire) influenced their decision for the education funds. The two major factors were John and Betty's ages and the children's ages.

For the tax minimization objective, both the Clifford Trust and Crown Loan received preference - 43.6% for each. The CPAs were fairly evenly split between the two but the attorneys chose Clifford Trust nearly twice as often as the Crown Loan for this objective. Three out of the four "CPA-Attorney" group felt the Crown Loan was the best device for saving on taxes.

The following table shows the preferences on the retirement funding:

<table>
<thead>
<tr>
<th>Estate Planning Devices</th>
<th>Retirement Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crummey</td>
<td>Clifford</td>
</tr>
<tr>
<td>CPA</td>
<td>16.7%</td>
</tr>
<tr>
<td>Attorney</td>
<td>5.9%</td>
</tr>
<tr>
<td>Both</td>
<td>0</td>
</tr>
<tr>
<td>TOTALS</td>
<td>10.3%</td>
</tr>
</tbody>
</table>

As shown, the CPAs and attorneys did not feel these three tools were the most effective methods for solving the Carlson's retirement objectives. Some of the "other" methods suggested by the respondents will be pointed out in the Analysis section.

The question dealing with the trust principal evoked interesting results.

<table>
<thead>
<tr>
<th>Trust Principal</th>
<th>CPAs' Preference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>16.7%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>38.9%</td>
</tr>
<tr>
<td>Securities</td>
<td>16.7%</td>
</tr>
<tr>
<td>Combination</td>
<td>22.2%</td>
</tr>
<tr>
<td>Other</td>
<td>5.6%</td>
</tr>
<tr>
<td>TOTALS</td>
<td>100%</td>
</tr>
</tbody>
</table>
Both groups agreed on the deciding factors for choosing between a trust and a loan. The availability of cash and the maturity and credit-worthiness of the children were the most frequent answers.

**Trust Principal : Attorneys' Preference**

<table>
<thead>
<tr>
<th></th>
<th>Cash</th>
<th>Real Estate</th>
<th>Securities</th>
<th>Combination</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>%</td>
<td>29.4</td>
<td>5.9</td>
<td>23.5</td>
<td>35.3</td>
<td>5.9</td>
</tr>
</tbody>
</table>

The years in practice affected the results on the education fund question in this manner:

**Years Experience : College Education**

<table>
<thead>
<tr>
<th></th>
<th>Crummey</th>
<th>Clifford</th>
<th>Crown</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 5 yrs.</td>
<td>20%</td>
<td>40%</td>
<td>40%</td>
</tr>
<tr>
<td>5 - 10</td>
<td>13%</td>
<td>38%</td>
<td>49%</td>
</tr>
<tr>
<td>10 - 20</td>
<td>-</td>
<td>50%</td>
<td>50%</td>
</tr>
<tr>
<td>Over 20</td>
<td>-</td>
<td>8%</td>
<td>92%</td>
</tr>
</tbody>
</table>

Thus the respondents years in practice did seem to have an effect on their answers to question 38:

"What factors have the most influence in this particular situation?"
(a) John and Betty's ages
(b) size of the estate
(c) children's ages
(d) more than one of the above
(e) other

The years of experience also affected the responses on the type of assets put into a trust. Most of the older respondents answered "other"
- listing insurance proceeds or a combination of cash, real estate and securities as the best solution.

For the question dealing with education, the respondents who had over 50% of their work concerned with estate planning chose Clifford Trusts. Those responding also felt that John and Betty's ages and children's ages were the most influential factors. The Crown Loan and Clifford Trust were both common answers to the tax minimization question by those survey participants with over 20% of their work in estate planning. The more experienced estate planners also felt these three methods were not the best choice for providing funds for the Carlsons' retirement. One asset was not preferred over another for trust corpus.

The participants that had more farm-related clients and experience in farm estate planning also chose Clifford Trust more frequently.

### Farm Estate Planning : Clifford Trust Preference

<table>
<thead>
<tr>
<th>% of Farm Estate Planning</th>
<th>Crummey</th>
<th>Clifford</th>
<th>Crown</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>42.9%</td>
<td>42.9%</td>
<td>14.3%</td>
</tr>
<tr>
<td>Less than 10</td>
<td>41.2%</td>
<td>47.1%</td>
<td>11.8%</td>
</tr>
<tr>
<td>10 - 20</td>
<td>20.0%</td>
<td>80.0%</td>
<td>0%</td>
</tr>
<tr>
<td>Over 20</td>
<td>10.0%</td>
<td>70.0%</td>
<td>20.0%</td>
</tr>
</tbody>
</table>

When the Crown Loan was chosen by the respondents, they felt the influencing factors included ages of parents and children and size of the estate. The question concerning the trust assets brought out varying opinions dealing with the two trusts for this example. For the Crummey Trust the results were as follows:

### Trust Principal : Crummey Trust

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>25.0%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>33.3%</td>
</tr>
<tr>
<td>Securities</td>
<td>8.3%</td>
</tr>
<tr>
<td>Combination</td>
<td>33.3%</td>
</tr>
<tr>
<td>Other</td>
<td>1.1%</td>
</tr>
</tbody>
</table>
There were two short answer questions on the survey. The first question asked for reasons for a selection of a trust or loan for the college funds. Some of the responses given for the Clifford Trust were to shift income to a lower tax bracket and maintain the right to get the money back. The Crummey Trust should not be used if an insurance policy was the trust principal. At John Carlson's age the insurance premiums would be too high for it to be a worthwhile choice. The Crummey "5 and 5" powers were also a factor in one respondent's choice of some other method over the Crummey Trust. A Clifford Trust is less beneficial to the Carlsons because of the ages of their children. They are too old to effectively utilize this method for college expenses. The Crown Loan was chosen for its flexibility and simplicity. The lack of liquid assets also was a major factor in several participants decisions making the Crown Loan a less attractive choice.

A variety of alternatives were listed for Question #12 dealing with the oldest son taking over the farm. There were a number of respondents who felt an incorporation might be best in this situation. Two types of stock would be used. The son would receive control through voting stock and the other four children would receive shares to provide financial equality. A limited partnership, land trust and a lease arrangement were other methods suggested.
Analysis of Statistics

After reviewing the results of the completed surveys and the comments on each question, some "solutions" for the Carlsons' financial objectives follow:

(1) The Crown Loan seems to be the most appropriate and effective planning tool for providing money for the children's education. With this method the parents will have control over these assets and have assurance that the funds will be used for college. If one of their children misuses the funds, the parents can demand repayment at anytime. This also will save taxes on interest by transferring this income to the children who are in lower tax brackets during the father's working years. Upon the father's retirement and after schooling is completed, the parent can call back the loans. This provides the additional funds for retirement which by now should be taxed at a lower rate. The legal fees and paperwork are reduced through the use of a Crown Loan.

(2) The ages of John, Betty and their children make it difficult for a Clifford Trust to be properly set up. If the Carlsons were not concerned about retirement funds, this may have been a possible option. The assets in the estate also play a part in the decision. A majority of the equity is in real estate. If this was tied up in a trust then they could not get to it for the retirement needs. Several respondents commented on the lack of cash but one participant replied that area banks readily loan
cash out (real estate as security) and parents in turn loan it to the children.

(3) The Crummey Trust was not chosen too frequently because of its complexity. Two of the attorney respondents had no knowledge of it. One individual stated that trusts often confuse the clients with their complexity so in certain cases a loan is preferred.

Another solution for college expenses and savings on taxes was to pay children for their farm labor (after school, weekends, and during the summer). This is a deductible expense and helps to reduce taxes for the parents. In this method the children are earning money for college and encourages responsibility and maturity.

The most common suggestions for the Carlsons' retirement funds were an IRA, Keough Plan, and a limited partnership. To allow the Carlsons' oldest son to take over the farm if he wishes, a number of respondents felt the Sub-Chapter S Corporation was an effective alternative. Common and preferred stock would be issued giving the oldest son voting control. Annual gifts of stock to children would spread the income to lower tax rates thereby reducing taxable estate. Upon the death of the parents the stock would be divided equally between the heirs, and the son could buy stock from his brother and sisters over his lifetime to obtain complete control of the farm. This alternative depends a great deal on the integrity and responsibility of the children. The Carlsons' children are still too young to make definite plans for the outcome of the farm. If the oldest son becomes mature enough to handle the farm operation, then this option may work effectively.

In comparison of responses of CPAs vs Attorneys the years of experience did affect the answers for education and tax savings. One
attorney commented that he felt no lawyer should act on these financial objectives without consulting a CPA. Most attorneys have not kept informed of all the tax law changes and tax rulings and thereby would not be competent counsel. Also many of the CPAs had a lack of experience in this area or other members of the firm handled the estate planning for their clients.

Concluding Comments

It appears the Clifford Trust and Crown Loan are the most favored estate and financial planning tools that practitioners would choose from the two trusts and the loan. The Clifford Trust is not as applicable in this particular illustration as it might be in a younger family's estate planning. Simplicity, flexibility, and ease of administration make the Crown Loan a wise choice when the funds are available. The use of the Crummey Trust is hampered by its limitations and complexity.

In summation, it is evident that the Carlsons must search for the most knowledgeable and informed CPA-Attorney to assist in the financial and farm estate planning needed for their objectives. It is a common conviction that the cost of estate planning is excessive. That inaccurate view has discouraged many a farmer from seeking professional advice. Actually a competent attorney and CPA can save a client in taxes many times the cost of developing his farm estate plan.
APPENDIX

EXHIBIT - 1

QUESTIONNAIRE
Please circle the letter corresponding to your answer.

1. What is your profession?
   a. C.P.A.
   b. Attorney
   c. Both

2. How many years have you been in practice?
   a. less than 5
   b. 5 - 10
   c. 10 - 20
   d. over 20

3. Most of your clients are involved in what type of occupation?
   a. professional services
   b. agricultural
   c. manufacturing
   d. other (specify) ______________________

4. What percentage of your client work deals with estate planning?
   a. less than 10%
   b. 10% - 20%
   c. 20% - 50%
   d. over 50%

5. What percentage of your clients seeking estate advice are involved with farming?
   a. 0%
   b. less than 10%
   c. 10% - 20%
   d. over 20%

Farm Estate Example

John Carlson and his wife, Betty ages 60 and 56, jointly own a 320 acre farm in Indiana. The Carlsons have five children ages: 21, 19, 18, 17, and 15. The three oldest are in college and the others in secondary school.

Their gross estate is valued at:

<table>
<thead>
<tr>
<th>Personal Estate</th>
<th>$150,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real Estate</td>
<td>650,000</td>
</tr>
<tr>
<td>Total Gross Estate</td>
<td>$800,000</td>
</tr>
<tr>
<td>Less: Debt</td>
<td>5,000</td>
</tr>
<tr>
<td>Life Insurance Proceeds on Husband and Wife</td>
<td>200,000</td>
</tr>
<tr>
<td>TAXABLE ESTATE</td>
<td>$995,000</td>
</tr>
</tbody>
</table>
Carlson's Financial Strategies: Minimize Taxes - 50% Tax Bracket
Provide Resources for their children's college educations
Maintain Adequate Retirement Funds

The parents want to provide funds for all children so they may go to college if they wish. The oldest son, age 17, plans to eventually take over the farm but wants to graduate from college first. John plans to retire at age 65. The approximate cost of college expenses per year for each child is $6,000.

In the following questions, use only the facts given in the farm estate example. Answer the questions with the intent of meeting the Carlson's financial strategies.

6. Which of the following financial planning tools would be most appropriate and effective in providing money for the children's education?
   a. Crummey Trust
   b. Clifford Trust (short-term trust)
   c. Crown Loan (interest-free loan)
   d. other (specify)

7. In question 6, why did you select this method over the others?

8. What factors have the most influence in this particular situation?
   a. John and Betty's ages
   b. size of the estate
   c. children's ages
   d. more than one of the above - if so, circle all items
   e. other (specify)

9. If the only goal was to minimize taxes which method would be best?
   a. Crummey Trust
   b. Clifford Trust
   c. Crown Loan
   d. other (specify)

10. What would be the best method for providing retirement funds for the Carlsons?
    a. Crummey Trust
    b. Clifford Trust
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    d. other (specify)
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   d. more than one of the above - if so, circle all items
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9. If the only goal was to minimize taxes which method would be best?

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   b. Clifford Trust
   c. Crown Loan
   d. other (specify) ______________________

10. What would be the best method for providing retirement funds for the Carlsons?

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<thead>
<tr>
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</thead>
<tbody>
<tr>
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<tr>
<td>Real Estate</td>
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<td>Total Gross Estate</td>
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<tr>
<td>Less: Debt</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>795,000</td>
</tr>
<tr>
<td>Life Insurance Proceeds on Husband and Wife</td>
<td>200,000</td>
</tr>
<tr>
<td>TAXABLE ESTATE</td>
<td>$995,000</td>
</tr>
</tbody>
</table>
11. If the Crummey Trust or Clifford Trust were chosen in this situation, what type of asset would you advise be placed in the trust as principal?
   a. Cash
   b. Real Estate
   c. Securities, etc.
   d. more than one of the above, if so, circle all items
   e. other (specify)

12. How should the Carlsons arrange for their oldest son to take over the farm operation and yet maintain financial equality?

13. In your past experiences, what do you find to be the deciding factor in choosing between the trusts and loans?
   a. availability of cash
   b. taxes
   c. maturity and creditworthiness of the children
   d. legal fees and paperwork
   e. other (specify)

14. Would you like a copy of the questionnaire results?
   a. yes
   b. no

Thank you very much for your cooperation!
FOOTNOTES


4. Friedman, p. 223.


6. Ibid., p. 462.

7. Ibid., p. 468.


10. Ibid.

11. Ibid.

12. Ibid., pp. 498 - 499.


23 Baldassari, p. 32.


26 Josephs, p. 31.


28 Baldassari, p. 33.

29 Ibid.

BIBLIOGRAPHY


Baldassari, Robert G. "Tax Planning to Cut College Costs: Which Technique is Best?" The Practical Accountant, August 1982, pp. 31 - 34.


