

Fraudulent Trusts

Every few years there seems to be a resurgence in the marketing of fraudulent trusts. You may hear about them from a client who asks you about a “pure business trust” or “constitutional trust” or some other name. They will have heard claims that this trust can save them from paying taxes, or make all their household expenses tax-deductible. As with most things in life, if it sounds too good to be true, it probably is. In fact, several years ago the IRS released a notice with that very title: “Too Good to Be True!” You can view or download it at <http://www.irs.gov/pub/irs-pdf/p2193.pdf>.

How to Spot a Fraudulent Trust

The IRS gives the following tips as ways to spot a questionable trust arrangement:

1. A promise to reduce or eliminate income and self-employment tax.
2. Deductions for personal expense paid by the trust.
3. Depreciation deductions on an owner's personal residence and furnishings.
4. Use of backdated documents.
5. Use of post office box for trust addresses.

The IRS warns against the following financial arrangements stating that they have been used to promote fraudulent trust schemes and do NOT provide any tax relief:

- 1) **Business Trust:** The transfer of an ongoing business to a trust, intending to make it appear that a taxpayer has given up control of that business. In reality, he or she still controls the day-to-day activities and income of the business.
- 2) **Equipment or Service Trust:** A trust formed to hold equipment that is leased to the business trust at inflated rates. The business trust reduces its income by claiming deductions for payments to the equipment trust.
- 3) **Family Residence Trust:** In this type of trust, the family residence, including furnishings, is transferred to a trust, which in some cases rents the residence back to the taxpayer. The trust deducts depreciation and the expenses of maintenance and operation, such as pool service and utilities.
- 4) **Charitable Organization Trust:** Assets or income are transferred to a trust claiming to be a charitable organization. The trust or “charitable organization”

pays for personal, educational, and recreational expenses for the taxpayer, claiming these payments are tax exempt.

5) **Foreign Trust:** A trust situated in a foreign country that imposes little or no tax on trusts while also providing privacy. When abused, this type of planning will cause taxable funds to flow through several trusts or entities until the funds are ultimately distributed or made available to the original owner. While claims are made that the distribution is tax free, the IRS's position is that the income is fully taxable.

Confusion = Opportunity

When word spreads about fraudulent trusts, it invariably causes a measure of unrest among our clients. This is an opportunity to explain that traditional estate planning trusts are not under attack. We don't want confusion to keep them doing appropriate planning!

It will ultimately require patience and the willingness to re-educate in order to allay our clients' fears.



KETRA A. MYTICH, LTD.

'Providing Peace of Mind for your and your loved ones'

On June 20, 2007 Ketra will be giving an Estate Planning Basics seminar. Please contact the office for further information.

For information on this seminar or if you would be interested in attending a future seminar, as well as setting up a seminar for your organization, please contact our office.

If you are interested in providing your clients with a copy of Ketra's book 'Your Life, Your Legacy' please call the office for complimentary copies.

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