

So, What's So Bad About LegalZoom, Anyway?

Not a week goes by that someone doesn't ask me about LegalZoom. You've probably seen the company's ads promising "common" legal documents at a fraction of what an attorney would charge. That claim has helped the company grow quickly, and last year they did at least 5,000 trusts. That doesn't even include the thousands of incorporations, trademarks, copyrights and other documents they've prepared for people.

In terms of sheer volume, they would be one of the largest law firms in the country – that is, if they actually *were* a law firm. But, they are not. That simple fact – and all that goes with it – is why I decided to write this article.

See, LegalZoom has grown too large and too popular to ignore. Someone must speak out about the danger that they represent and warn people who might otherwise get caught in their trap.

If you've heard their ads, I know what you're probably thinking...

"But, Robert Shapiro said the company was founded by lawyers, so we can be sure the documents are reliable. How can they be dangerous?"

The simple answer to that question is that it doesn't matter whether they were founded by lawyers or door-to-door vacuum salesmen. They aren't a law firm, and they can't give legal advice. They are what's referred to in California as "Legal Document Assistants." The requirements for becoming a Legal Document Assistant, or LDA, are essentially non-existent. A person seeking registration as a LDA must have a high school diploma and two years of education or experience in the legal field. Also, you will be glad to know that there is also the *very strict* requirement that they not be a felon. (Unofficial LDA motto: "No more than three DUI's, or you're out!")

Because the LDA is not an attorney, they are not allowed to give legal advice. The following paragraph is taken directly from the California LDA website:

We cannot give advice. We cannot give opinions, i.e. the client asks, "what would you do in my situation?" We cannot answer that question. The best defense is to tell them that you "do not have an opinion" and could not give it if you did. That they know their situation better than you do and if they need advice or an opinion, they must contact an attorney. We cannot select forms; however, we can provide them with the CALDA brochures and other published materials, which explain the procedures and list the forms needed. We cannot provide them with strategies. If they need a strategy, they must contact an attorney. After obtaining the information from an attorney, they can come back to a legal document assistant or unlawful detainer assistant to prepare the paperwork.

So, from an LDA you get no advice, no opinions and no strategies. They aren't even supposed to help you select the right form. Basically, the only thing they are allowed to do is take the information you provide and type it directly into the form.

But, wait a minute. LegalZoom was founded by attorneys. Doesn't that mean they can bend the rules a little and give you some advice?

Nope.

In fact, it virtually guarantees that you don't get any advice. Robert Shapiro and his friends at LegalZoom aren't stupid enough to risk their law licenses by giving legal advice through a company that is only registered as an LDA. To be clear, if LegalZoom were to give you legal advice, it would constitute a misdemeanor violation of Business and Professions Code § 6125-6127. For an attorney, a conviction for unauthorized practice of law is grounds for disbarment. (Yes, attorneys can be found guilty of unauthorized practice of law.)

See, one opinion, one strategy or one piece of advice, and Robert Shapiro may have to advertise that LegalZoom was founded by ex-attorneys.

At least with other LDAs who aren't so prominent, you run the chance that the poor schlub messes up and actually tells you something useful. With LegalZoom, you are completely hanging in the wind.

So, how do they do it, then? How do they prepare thousands of documents without giving any legal advice?

Well, I don't know enough about trademarks or copyrights to answer that question in general. But, when it comes to living trusts, the way they do it is to create a document that is so generic that it can apply to anyone. And, if there is an area where legal advice is necessary, they leave it out of the document, or they draft around the issue. Either way, you get a living trust that is no more sophisticated than the fill-in-the-blanks forms you can buy for \$14.95 at Staples.

That last point was important, so I'll repeat it. If there is any area that requires legal advice, they actually leave that item out of the document. In one instance I'll discuss in a moment, they actually give you incorrect information in order to avoid the possibility of giving legal advice.

Still, what amazes me is that I've explained this to dozens of people, and they almost always respond, "But, I'm not that complicated. Maybe generic is good enough for my situation. Isn't it." Of course, the irony of that question is that if you were to ask LegalZoom to answer it, the company would be breaking the law if they did.

So, as a real attorney, I will answer it. The answer is unequivocally that there are some people out there who would do just fine with a generic living trust. By "just fine" I mean that with a LegalZoom living trust, your head won't spontaneously

explode and your clothes won't catch fire. Odds are, your cholesterol numbers won't suddenly spike, and I'm reasonably sure that small children won't point at you in public and laugh at your mistake.

Heck, the LegalZoom trust might even help you avoid probate. That is, if you figure out what to do after you create the document – without any advice, opinions or strategies, of course.

To illustrate my point, I decided to log on to LegalZoom as a customer and go through the process to see what I got. Rather than use a hypothetical client, I decided to use my own family. We're pretty basic, and it saves me from the accusation that I intentionally created a family situation that LegalZoom does poorly with.

I'm 39 and married. We have a home. My business is a Subchapter "S" Corporation. I have an individual retirement account, and my wife has a 401(k) from work. We have two boys together, and I have a son from a prior marriage. Oh, and I have a dog. She's a boxer, if that matters.

That's it. That's my family in a nutshell. So, how badly could LegalZoom screw it up? Well, as you are about to see, pretty badly.

I created a LegalZoom account. And, after entering some basic family information, the website asked me to enter details about my assets. When I got to the section where I would enter my business, I selected the "help" button to see what it would say. Well, it told me that I can't put S-Corp stock into a living trust. There wasn't an explanation of what I was supposed to do with the S-Corp – just a statement that it can't go into my trust. I suppose that it is just supposed to go through probate.

But, probate isn't the real problem with that statement. The problem is that the statement isn't actually true. It's flat wrong. I'd like to be kind and tell you that it's a little-known fact and that they just made a mistake. But, I can't.

The truth is that S-Corp stock can go into a living trust quite nicely. The rules are found in Internal Revenue Code § 1361(d)(3). They even have a name for it. It's called a Qualified Subchapter "S" Trust, or QSST for short. (We tax lawyers love our acronyms.) However, it turns out that the guidelines in the Internal Revenue Code are just about impossible to meet in a generic plan. In other words, putting S-Corp stock in a living trust requires advice, opinion or strategy, and LegalZoom can't do that.

So, instead they give you incorrect information and hope you don't know any better.

For a LegalZoom customer who owns S-Corp stock, there are two possibilities. First, if they don't access the help screen, then transferring their S-Corp stock to the trust could blow Subchapter "S" status and convert the corporation to a C-

Corp. Or, if they do read the help screen, they leave the corporation out of the trust and it goes through probate. So, there are two possible results - both bad.

Next, I got to the section dealing with our retirement accounts. The website keenly told me that I can't transfer my retirement account into the trust. But, it also suggested that I could name the trust as a beneficiary of the retirement account. While that is technically true, it also is a decision that carries with it some pretty severe tax consequences if you don't do it just right. The odds of you doing it correctly without advice, opinion or strategy are about the same odds that your nine-year-old will suddenly discover nuclear cold fusion in the back yard while trying to create the Bellagio fountain using a soft drink and Mentos candies. In other words, you are going to blow it. I promise.

So far, LegalZoom would have cost me tens of thousands in probate fees and potentially hundreds of thousands in taxes.

It gets worse. Under my LegalZoom trust, my oldest son – the one from a prior marriage – is virtually guaranteed to be disinherited if I die before my wife.

And, these issues are just scratching the surface. I'm not even blaming LegalZoom for missing the tricky stuff like preserving our property tax basis for our children, figuring out what to do with my business after I die, protecting my children's inheritances from divorce and frivolous lawsuits, or ensuring that I avoid a conservatorship if I become incapacitated.

All of these issues could easily be avoided by hiring a competent estate planning attorney. And, true, your issues may be somewhat different, but everyone has issues that are beyond the capabilities of LegalZoom. Perhaps, a LegalZoom trust won't cause a tragedy for your family, but it's almost a certainty that there will be problems or missed opportunities.

Please, take my advice. Don't put your family at risk by preparing generic documents without the advice and counsel of a competent estate planning attorney. The extra money you spend will be more than worth it.

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