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## WHAT IS A REVOCABLE LIVING TRUST?

A **Revocable Living Trust (“Trust”)** is an agreement that determines how a person’s property is to be managed and distributed during his or her lifetime and at death.

A **Trust** normally involves three parties:

- a. *The Settlor or Grantor* – The person who creates the Trust, and usually the only person who provides funding for the Trust.
- b. *The Trustee* – This is the person who holds title to the Trust property and manages it according to the terms of the Trust. The Grantor often serves as Trustee during his or her lifetime, and another person or a corporate trust company is named to serve as Successor Trustee after the Grantor’s death or in the event the Grantor is unable to continue serving for any reason (i.e. illness, disability etc.).
- c. *The Beneficiary* – This is the person(s) who receive the income or principal from the Trust. This can be the Grantor (and the Grantor’s spouse) during the Grantor’s lifetime, and the Grantor’s spouse and/or children (or anyone else the Grantor chooses to name) after the Grantor’s death.

### BENEFITS OF HAVING A REVOCABLE LIVING TRUST

#### 1. *Probate Avoidance*

Having a Trust helps you avoid the time and expense of the probate process by managing your assets during your lifetime. (See **Common Misconceptions**) Assets in a Trust do not need to go through probate. Various examples of probate avoidance include:

- Property held in a Trust at the time of the Grantor’s death is not subject to probate administration, thus saving in probate expenses.
  - Property can be distributed to the beneficiaries shortly after the Grantor’s death, avoiding much of the delay encountered with probate administration.
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- Property out-of-state can be transferred to the Trust to avoid probate later. For example, if a Michigan resident also owns real estate in Florida, then upon his death it will be necessary to conduct estate settlement proceedings in both states. If, however, the Florida real estate is transferred to the Trust before the Grantor's death, the probate estate administration in Florida can be avoided.
  - If a Grantor becomes physically or mentally incapacitated, property held in Trust remains available to the Grantor without the requirement of a court-supervised guardianship or conservatorship.

## **2. *Reduces Estate Tax Planning***

During the Grantor's lifetime, the Trust has no effect on the annual income taxes which the Grantor will owe. In fact, if the Grantor is the Trustee or Co-Trustee, all income earned on assets held in the Trust is reported directly on the Grantor's income tax return and the Trust is not required to file a return. After the Grantor's death, the Trust is taxed at the same rate as a probate estate, which is generally the highest income tax rate. Usually all of the income from the Trust will be distributed to the beneficiaries to minimize the income tax consequences.

Proper planning can help reduce the amount of tax payable upon the Grantor's death. This can be accomplished through proper drafting and lifetime funding of the Trust for estate tax planning. A funded Trust can be used to transfer the federal estate tax exclusion amount (\$5,490,000.00 and indexed for inflation) to family members estate tax free.

## **3. *Helps Manage Distribution Planning***

A simple Last Will and Testament ("Will") can be limiting in terms of how assets are transferred to heirs. Some planning issues to consider are: whether heirs are to receive equal or unequal shares; at what age heirs should receive their shares, as well as whether they should receive assets all at once or in installments; what to do when an heir is disabled or has reckless spending habits; and how to assure that heirs will use their respective shares toward specific ends, such as to pay for a college education. A Trust offers more control over how assets will transfer to heirs than either a Will or beneficiary designation.

Having a Trust to help manage how assets are transferred is extremely beneficial, especially when dealing with **minor children**. State law entitles the minor children to obtain the funds outright at 18 (age of majority); whereas in a Trust, you can build your own parameters and guidelines pertaining to the age brackets and times at which the children are entitled to the funds. For instance, you could indicate that your children receive half of the funds in the Trust at age 23 and the remainder at age 30. You could also indicate that your children are not entitled to the funds until they are finished with college, and whatever age that is becomes the time at which they are entitled to the remaining funds. Under the guidance of an attorney, a Trust enables you to basically configure any distribution guidelines for your children that are comfortable for you.

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## COMMON MISCONCEPTIONS

Many people fail to complete or misunderstand the set-up process of a Trust. In other words, once an attorney sets up the Trust, assets are not automatically retitled so that the Trust becomes the asset owner. Some tips on properly funding your Trust are:

- Assets such as real estate, bank and savings accounts, investments, business interests, and notes payable to the Grantor should be immediately transferred to the Trust.
- Assets which have a tax deferred element to them like 401(k)s, IRAs, etc., should remain titled in the name of the Grantor; the beneficiary designation may name the Trust as either the primary or contingent beneficiary.
- If the estate is small enough that estate taxes are not a concern, the Trust can be both owner and beneficiary of life insurance policies to give the Trustee maximum control over the policies and proceeds.
- Property such as artwork, jewelry, cameras, and other household goods typically do not have a formal title. The attorney should prepare an assignment to transfer these items to the Trust.
- If a Grantor forgets to retitle some assets, they may be transferred to the Trust at death through a “pour over will.” (These assets will likely still have to go through probate.)
- The Trust will not act as an asset protection vehicle and avoid the claims of creditors, including Medicaid issues.

A Trust requires monitoring to ensure that assets remain in the Trust and that any newly purchased assets are titled in the Trust. For instance, a Grantor who transfers funds to a second financial institution must remember to advise the new institution to title the new account in the name of the Trust. Thus, it is important to carry out the proper funding of your Trust in order to help avoid probate. The important provisions to review every few years are who are your successor Trustees, when do your beneficiaries receive assets after your death, and are your assets titled properly to take advantage of the probate avoidance and estate tax planning. Failing to review your documents will only create problems for your heirs in the future.

Having a Trust prepared is part of a comprehensive estate plan. A Trust along with the pour over Will provides the necessary documents for estate administration at your death. Each person should also have a General Durable Power of Attorney and a Durable Power of Attorney for Health Care to allow their appointed agents to handle their business and medical affairs upon their incapacity.

In the event you would like to discuss any of these topics, please contact us for a complimentary consultation.



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