

Understanding Trusts

Answers to common questions

But how do you know if you need a Trust?

How do Trusts work?

How are Trusts set up?

How much does one cost?

Who should serve as Trustee?

These are just a few of the most frequently asked questions about Trusts.

How you can avoid probate, save taxes and more.

UNDERSTANDING TRUSTS

Frequently Asked Questions about Trusts

Whether you're seeking to manage your own assets, control how your assets are distributed after your death, or plan for incapacity, Trusts can help you accomplish your estate planning goals. Their power is in their versatility – many types of Trusts exist, each designed for a specific purpose.

What is a Trust?

A Trust is a legal entity that is created to hold assets for the benefit of another. A Trust is like a container that holds money or property for someone else. There are three parties in a Trust arrangement:

- The grantor (also called a settlor or Trustor): The person(s) who creates and funds the Trust
- The beneficiary: The person(s) who receives benefits from the Trust, such as income or the right to use a home, and has what is called equitable title to Trust property
- The Trustee: The person(s) who holds legal title to Trust assets, administers the Trust, and has a duty to act in the best interest of the beneficiary

You create a Trust by executing a legal document called a Trust agreement. The Trust agreement names the beneficiary and Trustee, and contains instructions about what benefits the beneficiary will receive, what the Trustee's duties are, and when the Trust will end, among other things.

Who Needs a Trust?

Not everyone needs a Trust, but most people should consider one. Trusts are not just for the rich. Setting up a Trust is an excellent way to control what happens to your estate, regardless of size, to possibly reduce estate taxes and protect against the expense and aggravation of probate.



I have a Will. Why would I want a Living Trust?

Contrary to what you've probably heard, a Last Will and Testament may not be the best plan for you and your family – primarily because a Last Will and Testament does not avoid probate when you die. A Last Will and Testament *must* be verified by the probate court before it can be enforced, and provides instructions for how your probate will be handled.

Also, because a Last Will and Testament can only go into effect *after* your death, it provides *no* protection if you become physically or mentally incapacitated. So the court could easily take control of your assets *before* you die by appointing a guardian to make decisions for you – a concern of millions of older Americans and their families.

Fortunately, there is a simple alternative to a Last Will and Testament – a *Revocable Living Trust*. It can avoid probate, and lets you keep control of your assets while you are alive even if you become incapacitated – *and* after your death.

Will or Trust? Which is best?

Most people need both. A big advantage of a Trust is that it is often the best strategy to avoid probate and to protect financial privacy. Last Wills and Testaments must be validated by probate court, a lengthy and expensive process that can take from six months to two years and, in some cases, even longer. Probating a Will may involve attorney's fees, personal representative's fees, administrative and other court costs. Unlike Wills, Trusts are not subject to probate and therefore enable you to keep your affairs private and minimize settlement costs and estate taxes.

What is probate?

Probate is the legal process through which the court sees that, when you die, your debts are paid and your assets are distributed to your beneficiaries according to the terms of your Will. If you don't have a valid Will, your assets are distributed according to state intestacy laws.

What's so bad about probate?

It can be expensive. Legal/Personal Representative fees and other costs must be paid *before* your assets can be fully distributed to your heirs. Costs vary in each state, but are usually estimated 3-8% of an estate's value. If you own property in other states, your family could face multiple probates, each one according to the laws in that state.

It takes time, usually 9 months to 2 years. During part of this time, assets are usually frozen so an accurate inventory can be taken. Nothing can be distributed or sold without court and/or personal representative approval. If your family needs money for living expenses, they must request a living allowance, which could be denied.

Your family has no privacy. Probate is a public process, so any "interested party" can see what assets you owned and to whom you owed debts. This process "invites"



disgruntled heirs to contest your Will and can expose your family to unwanted solicitations.

Doesn't joint ownership avoid probate?

Not really – it usually just *postpones* it. With most jointly owned assets, when one owner dies, full ownership *does* transfer to the surviving owner without probate. But when that owner dies without adding a new joint owner, or if both owners die at the same time, the asset must be probated before it can pass to heirs.

Watch out for other problems. When you add a co-owner, you lose control. Your chances of being named in a lawsuit and of losing the asset to a creditor are increased. There also could be gift and/or income tax problems. And since a Will does not control most jointly owned assets, you could inadvertently disinherit your family.

With some assets, especially real estate, all owners must agree to sell or refinance. So if a co-owner becomes incapacitated, you could find yourself needing to involve the court, even if the ill owner is your spouse.

Why would the court get involved at incapacity?

If you can't conduct business due to mental or physical incapacity (Alzheimer's, stroke, heart attack, etc.), only a court appointed guardian can execute documents for you – even if you have a Will. (Remember, a Will only goes into effect *after* your death.)

Once the court appoints a guardian, the guardianship continues until you regain your capacity or die. The court, not your family, controls how your assets are used to care for you. This public process can be expensive, embarrassing, time consuming and difficult to end if you recover. And it does not replace probate at death – your family could have to go through the court system *twice*!

Does a durable power of attorney prevent this?

A durable power of attorney lets you name someone to manage your financial affairs even after you become incapacitated. However, many financial institutions won't honor one unless it's on *their* form. And, if accepted, it may work *too* well –it can simply give someone a “blank check” to do whatever the Agent wants with your assets. It can be very effective when used in addition to a Living Trust, but risky when used alone.

How does a Living Trust avoid probate and prevent court appointment of a guardian?

When you set up a Living Trust, you transfer assets from *your* name to the name of *your Trust*, which *you* control.

Legally you no longer own any assets (everything now belongs to your Trust), so there is nothing for the courts to control when you die or become incapacitated. The concept is very simple, but this is what keeps you and your family out of the court system.



Do I lose control of the assets in my Trust?

Absolutely not. You keep full control. As Trustee of your Trust, you can do anything you could do before – buy and sell assets, amend or even revoke your Trust (that's why it's called a *Revocable Living Trust*). You even file the same tax returns. *Nothing changes but the names on the titles of your assets.*

Funding a Trust

You can put almost any kind of asset in a Trust, including cash, stocks, bonds, bank accounts, real estate, and artwork. The assets you choose to put in a Trust will depend largely on your goals. For example, if you want the Trust to generate income, you should put income-producing assets, such as bonds, in your Trust. Or, if you want your Trust to create a fund that can be used to pay estate taxes or provide for your family at your death, you might fund the Trust with the proceeds of a life insurance policy.

Potential Trust Advantages:

- Avoid the expense and delay of probate
- Preserve assets for your children until they are grown (in case you should die while they are still minors)
- Create a pool of investments that can be managed by professional money managers
- Set up a fund for your own support in the event of incapacity
- Shift part of your income tax burden to beneficiaries in lower tax brackets
- Provide benefits for charities

Potential Trust Disadvantages

- There are costs associated with setting up and maintaining a Trust, which may include Trustee fees, professional fees, and filing fees
- Depending on the type of Trust you choose, you may give up some control over the assets in the Trust
- Maintaining the Trust and complying with recording and notice requirements can take considerable time
- Income generated by Trust assets and not distributed to Trust beneficiaries may be taxed at a higher income tax rate than your individual rate
- While there may not be any probate fees, your successor Trustee may require the assistance of an attorney to complete distribution of the Trust assets

Types of Trusts

There are many different types of Trusts, the most basic being revocable and irrevocable. The type of Trust you should use will depend on what you're trying to accomplish.



Living (revocable) Trust (also known as an Inter Vivos Trust)

A living Trust is a Trust that you create while you're alive.

A living Trust:

- Avoids probate: Unlike property that passes to beneficiaries by your Will, property that passes by a living Trust is not subject to probate, avoiding the delay of property transfers to your beneficiaries and keeping matters private.
- Maintains control: You can change the beneficiary, the Trustee, any of the Trust terms, move property in or out of the Trust, or even terminate the Trust and get your property back at any time.
- Protects against incapacity: If because of an illness or injury you can no longer handle your financial affairs, a successor Trustee can step in and manage the Trust property for you while you recover. In the absence of a living Trust or other arrangement, your family may have to ask the court to appoint a guardian to manage your property.
- A living Trust can also continue after your death – you can direct the Trustee to hold Trust property until the beneficiary reaches a certain age or gets married, for instance.

Caution: *Despite the benefits, living Trusts have some drawbacks. Property in a living Trust is generally not protected from creditors, and you cannot avoid estate taxes using a living Trust.*

Irrevocable Trusts

Unlike a revocable Trust, you can't easily change or revoke an irrevocable Trust. You usually cannot change beneficiaries or change the terms of the Trust. Irrevocable Trusts are frequently used to minimize potential estate taxes. The transfer may be subject to gift tax at the time property is transferred into the Trust, but the property, plus any future appreciation, is usually removed from your gross taxable estate.

Additionally, property transferred through an irrevocable Trust will avoid probate, and may also be protected from future creditors.

Is a Living Trust expensive?

Not when compared to the costs and loss of control that come with court interference at incapacity and death. How much you pay will depend on how complicated your estate plan is. Be sure to ask for an estimate in advance.

How long does it take to get a Living Trust?

It should only take a few weeks to prepare the legal documents after you make basic decisions, then meet with an attorney to sign the Trust Agreement.

Should I have an attorney prepare my Trust?

Yes. An experienced attorney can provide valuable guidance and assistance, and assure your Trust is drafted properly.



If I have a Living Trust, do I still need a Will?

Yes, a Pour Over Will acts as a kind of “safety net,” in the event you forget to retitle an asset in the name of your Trust. Upon your death, the Will “catches” the forgotten asset and directs it into your Trust. The asset may still have to go through probate first, but at least it can then be distributed as part of your Living Trust plan of distribution.

Who should have a living Trust?

It doesn't matter how old you are, how much you own, or if you're married or single. If you own any assets and you want to make sure your loved ones (spouse, children or parents) will avoid the problems of court interference at your death or incapacity, you should also consider a Living Trust. You may also want to encourage other family members to have one so *you* won't have to deal with the courts at their incapacity or death.

Should I consider naming a Corporate Trustee?

You may decide to be the Trustee of your Trust. However, some people select a Corporate Trustee (bank or Trust company) to act as Trustee or Co-Trustee now, especially if they don't have the time, ability or desire to manage their Trusts, or if one or both spouses are ill. Corporate Trustees are experienced investment managers, they are objective and reliable, and their fees are usually very reasonable.

Benefits of a Trust

- Avoids probate at death
- Avoids multiple probates if you own property in more than one state
- Prevents court control of assets at incapacity
- Brings all of your assets together under *one* plan
- Provides maximum privacy
- Quicker distribution of assets to Beneficiaries
- Assets can remain in Trust until Beneficiaries reach the age(s) *you* want them to inherit funds
- Can reduce or eliminate estate taxes
- Inexpensive, easy to set up and maintain
- Can be modified or cancelled at any time
- Difficult to contest
- Prevents court from controlling assets when minor children inherit
- Can protect dependents who are disabled
- Prevents unintentional disinheritance and other problems of joint ownership
- Professional asset management if you use a corporate Trustee
- Peace of mind

Please call our office at (727) 327-7600 to schedule an appointment to discuss your particular needs and how a Trust can help to accomplish your estate planning objectives.

