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REVOCABLE LIVING TRUSTS

Revocable Living Trusts (RLTs) are popular estate planning tools. The purpose of this article is not to provide a legal treatise on the subject of RLTs, but rather to introduce you to how they work, some of their benefits and drawbacks, and some important considerations when creating an RLT.

RLT Basics

An RLT is a written legal agreement involving three parties: the Trustmaker (also known as a Grantor, Trustor or Settlor), the Trustee and the Beneficiary. Initially, upon its creation, the Trustmaker, Trustee and Beneficiary are one in the same person. Moreover, there can be, and often are, more than one Trustmaker, Trustee and Beneficiary at any given time. [Note: Depending on the law of their jurisdiction and their unique circumstances, a married couple may share one joint RLT or each may have separate RLTs.]

After the Trustmaker and Trustee sign the RLT legal agreement, the Trustmaker funds the RLT (i.e., retitles assets into the name of the RLT). This is a critical step, much like putting fuel into a brand new automobile. Once the RLT is signed and funded, the Trustee manages and distributes the RLT assets for the Beneficiary according to the instructions in the written legal agreement.

Later, if the Trustmaker/Trustee becomes incapacitated, as defined in the RLT agreement, then the successor Trustee appointed in the RLT seamlessly manages and distributes RLT assets for the Trustmaker/Beneficiary based on instructions in the RLT agreement itself. Since the Trustee holds legal title to the RLT assets for the Beneficiary, no Probate Court need interfere in the financial affairs of the incapacitated Trustmaker/Beneficiary.

Finally, upon the death of the Trustmaker/Trustee/Beneficiary the RLT becomes irrevocable and the successor Trustee seamlessly manages and distributes RLT assets for the successor Beneficiary according to the instructions in the written legal agreement. In most jurisdictions, no Probate Court need interfere in this process of transferring assets to the RLT successor Beneficiary.

RLT Benefits

While the benefits of RLT-based planning vary from jurisdiction to jurisdiction, the most commonly cited RLT benefit is Probate Court avoidance. And the three most commonly cited drawbacks to Probate Court are the potential for unnecessary delays, costs and publicity. Given the choice, most people would rather avoid any court process.

RLT Drawbacks

As previously noted, for an RLT to operate as designed it must be funded. If you are not meticulous in ensuring that your RLT has either present title to your assets or will have future title to them (e.g., life insurance proceeds), then your estate may not avoid Probate Court. Also, legal fees to create RLTs often are higher than the fees to create Will-based estate plans. Accordingly, in some jurisdictions the benefits of avoiding Probate Court are greater than in other jurisdictions.

RLT Considerations

The selection of your successor Trustee is one of the key decisions you must make when creating your RLT. Common options include appointing a trusted family member/friend, a professional fiduciary, or even a combination of the two. There is no right answer, just the one that is right for you.

Make sure your RLT incorporates flexible federal estate tax planning. Your RLT should be drafted to provide maximum protection from this form of taxation. Even if the estate tax is repealed, it can always be reinstated. Warning: Some states may impose their own inheritance or estate taxes, too!

Finally, only you know the strengths and weaknesses of your loved ones. Ensure that your RLT contains special planning to protect the inheritance both for and from your loved ones, as may be necessary. If you are divorced, then you might wish to ensure that your ex-spouse does not inherit through your mutual children, too.

Asset Re-Titling

Asset re-titling (also known as trust funding) is the process of placing your assets under the ownership and control of your Revocable Living Trust (RLT). It is a vital component of any RLT-based estate planning process. Only those assets that are titled in the name of your RLT (or that designate your RLT as beneficiary, where appropriate) will be controlled by the terms of your RLT. Otherwise your assets may be subject to probate, may lose valuable protection from estate taxes and may not pass to your beneficiaries as specified in your estate plan.

There are three fundamental steps in the Trust Funding process:

1. Identify all of your assets by:
    - Type: For example, is this asset a bond certificate, a certificate of deposit, or a publicly-traded stock certificate?
    - Value: How much is it worth and is it encumbered by debt?
    - Ownership: Do you own it individually or jointly with a spouse or others?
2. Transfer ownership to your RLT:

Once you have identified your assets, you can begin transferring ownership to your RLT by sending written notice to the various institutions involved. In that notice you identify the asset, the name of your RLT and then request the change of ownership or beneficiary designation. Note: Do not be surprised if they respond with a request for completion of their own in-house form.

3. Maintain your Trust Funding:

As you acquire additional assets, be sure to title them in the name of your RLT or use the appropriate beneficiary designation from the outset.

Here is a review of some assets that require special (and careful) attention when funding your RLT (now or by beneficiary designation).

<u>Real Estate</u>

Your Personal Residence: Even if there is a mortgage against your residence, federal law (The Garn-St. Germain Depository Institutions Act of 1982) allows you to transfer your residence to your RLT when the loan is federally-backed.

Other Real Estate: If you have debt against any other type of real estate, first contact the lender to obtain permission to transfer ownership to your RLT. The federal law protecting transfer of your personal residence does not extend to your investment real estate. Failure to obtain prior approval could result in an acceleration of payments.

<u>Beneficiary Designations</u>

Life Insurance: If you name your RLT as the beneficiary of all of your existing and future life insurance policies, then the proceeds will be administered and distributed according to the terms of your RLT. [Note: Because the death proceeds will be included in the value of your estate, consideration should be given to establishing an Irrevocable Trust as owner and beneficiary to remove the death proceeds from your estate subject to certain rules.]

Qualified Retirement Plans: There are many complex tax and non-tax consequences attending any beneficiary designation option you may select. Bottom line: Make no decision without appropriate legal counsel. One mistake could spell disaster!

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