SPECIAL REPORT

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Living Trusts - Facts and Fiction

With the increasing number of citizens utilizing Living Trusts, many states have adopted the Uniform Trust Code to facilitate the use of the Living Trust in Estate Planning. Pennsylvania adopted the Uniform Trust Act in 2006, while Ohio followed in 2007. But even in the midst of the popularity of Living Trusts, there still seems to be quite a bit of misinformation in the marketplace. Many articles have been written on the subject yet many people find it difficult to decide whether a Living Trust is right for them or not. Some writers claim that scam artists prey on consumers' fears that their estates will be eaten up by probate costs and the distribution of assets to their loved ones will be delayed. These writers seem to favor probate and claim Living Trusts are only for the very wealthy. These advocates issue the warning to "beware of non-attorneys selling Living Trusts." We agree that Living Trusts should not be prepared by anyone other than an attorney, but we have also seen a good number of attorneys advocating against Living Trusts without actually making sure their clients are fully educated about Living Trusts. This is as bad as the scam artists who sell trusts as a one-size-fits-all estate plan. The truth is that no one but YOU can decide if a Living Trust is the right Estate Plan. And the only way for YOU to decide is to be fully educated. An attorney who has never prepared a trust or an attorney whose practice depends heavily on clients with a Will whichs lead them through probate, shouldn't be deciding whether YOU should have a trust. Nevertheless, time and again we hear of stories from clients whose former attorney advised them against a Living Trust, but when asked why, could only say, "He told us we didn't have a big enough estate," or "She said that probate wasn't that expensive." They trusted the word of these attorneys, but in fact, how did these attorneys know? If having the estate go through probate doesn't cost that much, maybe these attorneys would be willing to do what the funeral directors are doing – allow clients to pre-pay the cost to go through probate. In our opinion, it is like telling someone they don't need life insurance without making sure the family understands WHY they don't need it. And that is the key to the facts and fiction of Living Trusts. You shouldn't have to take the word of ANYONE that a Living Trust is right or wrong for your family. Don't listen to someone tell you a Living Trust is good or bad without making sure they are ***qualified*** to discuss Living Trusts. Unfortunately, those who mislead will also be less than forthcoming about their expertise and their bias regarding Living Trusts. The court fee for probate in Ohio and Pennsylvania is typically less than $250 – not a great sum. The problem is citizens are being told this and are conveniently NOT being told that in addition to the court fee, attorneys typically charge up to 5% of the value of the estate for probate. And, probate comes in two varieties: Death Probate and Living Probate (also known as Guardianship). Will a Power of Attorney (POA) help you avoid a Guardianship? This is a critical question to ask the person advising you AGAINST a Living Trust. Do you know most states have no law requiring a third-party to honor a Power of Attorney? Most Banks won't accept a Power of Attorney, unless it is one the Bank provided. You may hear, "Guardianships are rarely needed." Tell that to just one person whose parent had a guardianship imposed on him or her. All it takes is just one financial institution to refuse to honor an incapacitated person's POA to make a Guardianship necessary. On the other hand, did you know that institutions cannot refuse to deal with the trustee of a properly funded Living Trust? Although this is a FACT, rarely is the avoidance of Guardian-ship emphasized by those who advocate against Living Trusts.

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WHAT IS A LIVING TRUST?

The working definition of a trust is a "legal instrument used for holding assets." Typically a trust is a legal document in written form created to hold and manage assets of one or more individuals. A living trust (also referred to as an ***intervivos trust***) is a trust established by a person during his or her lifetime, while a ***testamentary trust*** is established after death, usually as a result of instructions in the decedent's Will. A trust that holds assets is said to be a "funded trust." "Funding" a trust is accomplished by re-titling an individual's assets into the name of the trustee of the trust. For example, John and Mary Smith sign a joint trust document drafted by an attorney and, immediately thereafter, set about the task of changing the title of their assets from "John and Mary Smith" to "John and Mary Smith, Trustees of the Smith Trust.

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HISTORY OF TRUSTS

Trusts are said to date back to the Roman Empire; however, trusts in America, like the American System of Justice, are based on the English model. Prior to Britain's settlement of the colonies, only the aristocracy were landowners (landed gentry). English aristocrats used almost exclusively the trust to hold and manage their estates. When our American ancestors settled in the new world, land ownership suddenly became available to ordinary freemen. However, unlike the English aristocracy, the use of trusts by these freemen in planning their estates was not widespread. This did not become a problem for the colonists at first, since real estate was traditionally held in families from generation to generation. The problem only arose when descendants decided to transfer the real estate and realized that the land was in the name of an ancestor. Then it became necessary to request an order from the court authorizing the transfer of the land. Over the years the increasing requests for such orders resulted in a uniform set of procedures and a specialized civil division, the so-called Probate Court, to be established in the individual states. Because of the recent explosion in the number of citizens turning back to the way our English ancestors handled their estates, many states have adopted the Uniform Trust Code. Currently, 35 states and the District of Columbia have adopted the Uniform Trust Code. States which have not adopted a trust code rely upon a combination of statutes and common law to regulate how citizens manage their assets which are held in a trust. Statutes, including the Trust Code, are the body of laws enacted by the state legislature and are organized in a manner which is similar to an encyclopedia. The common law is the body of law made by court judgments and decisions by judges. Although attempts have been made to categorize these judgments and decisions for orderly research, one can imagine the enormous task of organizing hundreds of years of a state's court cases so that a particular question of law can be answered. Statutes are much easier to research because of their encyclopedic organization.

WHAT IS PROBATE?

The Probate Court in each county (Orphans' Court in PA) oversees the legal process that includes determining the validity of your Last Will & Testament (Will), gathering your assets, paying your debts, taxes, and the expenses of Will administration, and then distributing the remaining assets to those persons entitled to them. The surviving heirs are the usual parties who submit the Will to probate court. The main advantage of probate is the court supervising the entire proceedings, making sure all rules and laws are followed. The rules make it easier for creditors to make claims and third parties to make challenges to the will. Nevertheless, the probate process can be time consuming, costly and has been criticized for loss of privacy regarding the deceased's financial affairs as it is completely open to public inspection.

PROBATE PROCESS

The person you nominate as the executor in your Will many more times than not becomes the representative appointed by the court. The the court will oversee the executor to ensure the duties are carried out properly. Typically, the executor requires the assistance of an attorney to carry out the duties since whenever a would-be executor seeks to have questions answered at the courthouse, the mantra of every probate court clerk is, "we cannot give legal advice." To begin the probate process, the person nominated to be executor submits the Will to the probate court in the county where the decedent resided. The court will review the executor's residency and bond requirements, although most modern Wills request the bond be dispensed with. The expense of a bond is not waived when there is no Will (the decedent having died ***intestate***, as opposed to ***testate***). It is during the initial proceedings when the court takes into consideration any challenges to the Will. By the way, the testate process is a bit more stream-lined compared to intestate; if a decedent dies intestate, the court appoints an administrator whose duties are akin to the executor, but the process generally involves more time and effort. Once appointed, the executor/administrator collects and inventories the assets, pays debts and then distributes property as directed by the Will, or according to the intestate laws of the state if there is no Will.

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COST OF PROBATE

There can be substantial cost involved in probating an estate, so it makes sense to avoid or curtail full probate where possible and appropriate. Although the actual fees charged by the court are many times modest, probate also involves executor and attorney fees, which range from 4 to 5 percent of the probate assets and up to 1 percent of the non-probate assets, depending on the state where assets are located. Sometimes executors who are friends or family agree to serve without a fee. An attorney's fees will vary depending on the amount of work spent on the probate process, but they are usually based on the same guidelines.

LENGTH OF PROBATE

Probate proceedings can be lengthy. Many estates can take a year or two to complete, and if it's necessary to file federal estate tax returns, the proceedings can last well into a third year. The size of the estate and state laws affect the length of the probate process. The time it takes for distributions to reach beneficiaries also varies. The usual time frame for the first distribution is from four to eight months from the time of death, although most states have provisions for spouses and minor children to receive distributions almost immediately. The duration and cost of the regular probate process can be minimized for some small estates that do not exceed a certain value. Estates under $50,000 in Pennsylvania and under $35,000 ($100,000 if surviving spouse is sole heir) in Ohio qualify for an expedited probate process.

PRIVACY

When a Will is admitted to probate, it becomes public record. Not only does the Will become public, but all documents involved in the proceedings become public record and can be viewed by anyone. Some people have legitimate reasons for viewing this loss of privacy as a negative aspect of probate.

AVOIDINGPROBATE

A good way to relate to the probate process is to think about ownership of assets. If you own all your assets in your name (as opposed to holding your assets in a trust or a corporation, a limited liability company or some other entity) and you die, you can no longer transfer your assets – that is, you can't sign over the deed to a house, you can't endorse a stock certificate, a check or other titles. In this situation, the Probate Court is the only institution with the authority to transfer ownership from a deceased person to the living heirs. As a practical matter, the Probate Court's chief function is to oversee and authorize the transfer of assets after a death. Some assets can be titled in such a way as to be "payable on death" when you die (POD) and these assets escape the probate process; unless, of course, the POD beneficiary dies before the assset owner. If you pass away owning assets in your name without provision for the asset to pass to another individual, those assets will be administered by a probate court in the county where the asset is located. It is even possible to have multiple probates, especially if a decedent owns out-of-state property (typically time-share ownership is outside your state of residence). A very common way to avoid the probate process altogether is with a Living Trust and the transfer to the trust, while you are alive, of substantially all of your assets. Living Trusts are governed by their own provisions and they need not end immediately at your death. Therefore, if the trust is the titleholder to your property, there is no need to go through probate to re-title those assets after death. Instead, the successor trustee performs the same duties as an executor and then distributes the trust assets as you have specified in the trust. Life insurance, pension plans and retirement accounts can be payable directly to a named beneficiary, and will be neither governed by the Will nor require probate. Similarly, property owned jointly with survivorship rights passes automatically to the survivor and is not subject to the Will or probate proceedings. However, we strongly advise that the trustees of the Living Trust be designated as a contingent beneficiary on all life insurance policies, pension plans, and retirement accounts. And, we caution our clients that property owned jointly with survivorship rights with a spouse only avoids probate on the death of the first spouse; therefore, it is advisable to re-title these assets into a Living Trust in order to completely avoid probate.

For a Fair discussion of the Facts & Fiction of Living Trusts in Estate Planning, contact Attorney Val Holz

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