

Should I Have a Trust? - The Revocable Trust - Second in the Trust Series

This is the second Blog in the Trust Series. In last week's post, I described what a Trust is and the two general categories of Trusts – testamentary Trusts and *inter vivos* Trusts. I also pointed out that an *inter vivos* Trust can be either revocable or irrevocable. Finally, I defined some common Trust terms. You can click [here](#) to access the first Blog in the Trust Series. This week I will focus on some of the characteristics of revocable *inter vivos* Trusts.

A revocable *inter vivos* Trust (also known as “revocable trust” or “revocable living trust”) can be a very effective estate planning tool to manage assets during lifetime. A settlor can establish a revocable Trust, transfer his or her assets to the Trust during lifetime and serve as the sole Trustee of the Trust. In this situation, the settlor continues to manage his or her assets as before, but the assets are held in the name of the revocable Trust and the settlor is serving in the role of Trustee. Because the Trust is revocable and can be amended or terminated, functionally little has changed from the settlor's perspective. The trust agreement typically specifies that the assets and income will be used as directed by the settlor. The settlor retains all control over the assets held in the revocable Trust, in the role as Trustee, and can invest them, sell them, purchase replacement assets and transfer additional assets to the Trust, all without the consent of any third party.

In the trust agreement, the settlor will appoint one or more successors to assume the role of Trustee in the event that the settlor no longer wishes to continue to manage his or her financial affairs. The settlor can also appoint a Co-Trustee to serve with the settlor. One good example of the use of a revocable Trust for asset management is the case of a settlor who expects to travel outside the United States for an extended period of time, perhaps in less settled areas of the world, and wants to appoint a Trustee to manage and administer the assets while the settlor is traveling.

If the settlor becomes incapacitated, very little transition is needed to continue the asset management features of the revocable Trust. The settlor's assets continue to be held in the revocable Trust. The successor Trustee (or the Co-Trustee if one was serving with the settlor) steps in to manage the assets for the benefit of the incapacitated settlor (and, if desired, his or her family). The Trustee takes on the role of making and implementing financial decisions for the benefit of the settlor. The trust agreement will give the successor Trustee guidelines on how to apply and distribute the assets held in the Trust during the settlor's incapacity. The successor Trustee has the duty and responsibility to invest the assets in the Trust prudently and to provide accountings of the bills and expenses paid, investments made, assets sold and purchased and income earned.

During lifetime, the settlor will continue to pay the income taxes on the income and gains earned by the assets held in the revocable Trust. There is no income tax advantage (or disadvantage) to be gained from a revocable Trust during the settlor's lifetime. Moreover, a revocable Trust is not a Medicaid qualification planning vehicle – a settlor cannot make himself or herself eligible for Medicaid assistance with a revocable Trust.

If lifetime asset management is an objective in creating the revocable Trust, then title to certain of the settlor's assets typically would be transferred to the revocable Trust. The nature of the asset will dictate the method by which the title is transferred from the settlor to the revocable Trust. For example, if real estate is to be transferred to the revocable Trust, then the title transfer is generally accomplished with a real estate deed. In addition, certain types of assets, like real estate, require special attention before being transferred to a revocable Trust, including addressing issues related to mortgages on the real estate, title insurance and homeowner insurance.

There are many types of assets that a settlor cannot or would not transfer to his or her revocable Trust. For example, individual retirement accounts, 401(k) plan accounts and similar retirement assets that the settlor owns or participates in would not be transferred to the revocable Trust during lifetime. Rather, the proceeds of these accounts are paid at death to the person(s) listed in a separate beneficiary designation form provided by the provider or sponsor of the retirement account. Depending upon the circumstances and the settlor's goals and objectives, it might not be appropriate for the death benefits of these retirement accounts to be paid to the Trust on the settlor's death. Moreover, particular tax-sensitive assets, such as stock in an "S" corporation, will require that the revocable Trust agreement contain certain clauses so that the tax status of the asset is not jeopardized when held in the revocable Trust, particularly after the death of the settlor.

If the settlor creates a revocable Trust and becomes incapacitated before transferring assets to the Trust, an agent designated in a durable power of attorney signed by the settlor before incapacity occurs can be authorized to transfer assets to the revocable Trust.

A revocable Trust is often used as a "Will substitute" to direct who receives assets at death. The revocable trust agreement contains many of the same provisions that would be included in a Will. For example, additional trusts can be created in the revocable Trust agreement and funded at the death of the settlor with the property held in the revocable trust.

It is important to note that creating a revocable Trust as the cornerstone of an estate plan does not eliminate the need for a Will. Because the revocable Trust contains all of the clauses directing who receives assets on the death of the settlor, it is imperative that all of the settlor's assets be transferred to the Trust for distribution in accordance with the terms of the revocable Trust agreement. A Will, commonly referred to as a "pour over" Will, accomplishes this by directing that any property owned by the settlor that was not transferred to the revocable Trust during lifetime will be "poured over" and transferred to the revocable Trust at the settlor's death.

Upon the death of the settlor, the revocable trust becomes irrevocable. The beneficiaries of the Trust are entitled to receive notice about the existence of the Trust and can request information about the Trust property, how the Trust property is invested, the type and amount of expenses that are incurred and paid and the amount of, and to whom, distributions are made.

Under Colorado law, a Trust is required to file a Trust Registration Statement with the appropriate court if its principal place of administration is in Colorado and the Trust has certain characteristics. A fully revocable Trust is not required to file a Trust Registration Statement until

such time as the settlor's power to revoke the Trust has terminated. If all assets of the Trust are distributable outright to beneficiaries upon the settlor's death, then a Trust Registration Statement need not be filed. Numerous income tax rules come into play when the settlor of a revocable Trust dies; some of the same rules apply when a Will is the cornerstone of an estate plan.

Next week I will discuss some of the factors to be considered in deciding whether the cornerstone of an estate plan should be a revocable Trust or a Will.

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Barbara Ann Dalvano, Esq.
Phone and Text Message: (719) 963-2933
Email Address: barbaradalvano@yahoo.com

Feel free to visit our website at www.attorneybarbaradalvano.weebly.com.