Do We Need Revocable Living Trusts?

Clients, Friends and Website Visitors:

In my 20 plus years of legal practice one question clients and prospective clients continue to ask me is whether they need revocable living trusts or just standard wills as their primary estate planning tool. Unfortunately, there is no clear-cut correct answer to this question. The variables that would indicate the need for a revocable living trust over a standard will have changed as the years have passed. As such, I thought it might be beneficial to go through the purposes of a revocable living trust and how those purposes can be achieved as well as providing a brief primer on the current estate tax laws in the United States and how they apply to a couple's estate.

The primary purpose for a revocable living trust is to allow for the grantor (the person setting it up) thereof to dispose of his or her property upon his or her death without the necessity of going through probate. The main reason that people choose the route of a revocable living trust is to avoid the cost and publicity of having their assets go through a probate proceeding upon their death. However, this purpose can only be achieved if the assets owned by a grantor are transferred into the revocable living trust during the lifetime of the grantor.

Essentially, a revocable living trust splits the ownership and enjoyment of an asset between three separate entities. The first is the grantor who is the individual setting up a trust. The second is the trustee who is the individual or entity that actually owns the asset in the trust as a fiduciary and administers the trust. Finally the third entity is the beneficiary of the trust. Without a revocable living trust when an individual owns property individually or jointly, be at personal or real property, that individual is acting in all three of these capacities. Likewise, when an individual creates and funds a revocable living trust that individual will typically initially act in these same three capacities. Thus, during the individual's lifetime, provided he or she is not incapacitated, there is no functional difference between how the individual treats assets which are own individually or jointly and how such individual treats assets which are subsequently put into his or her revocable living trust. The difference occurs upon the individual's death.

When an individual dies owning property in his or her individual name the only way to get the title to such property into the name of his or her beneficiaries is by going through the probate process and have the title of the property transferred by the probate court from the decedent's name to the decedent's beneficiaries. When a person who has transferred his or her assets into a revocable living trust dies, the trust becomes irrevocable but continues on. The grantor has died but a successor trustee (remember the grantor was also the original trustee) steps in for the deceased grantor and his or her chosen beneficiaries become the new beneficiaries. However the ownership of the asset stays in the name of the trustee of the trust and as such there is no need to have the probate court step in and transfer the ownership of the asset. This is how the use of a revocable living trust avoids the probate proceeding.

The importance of this for most people is that the probate proceeding is somewhat costly in that the attorney's fees and personal representative fees associated with probating an estate are based upon a sliding scale percentage of the estate. In Missouri, the attorney's fees for probating a $1 dollar estate are $27,000. This is true even if the attorney does little more than open the estate. As you can imagine, it is this cost of probating an estate that led to the popularity of revocable living trusts which began in the 1970s and has continued through today. However, unlike most state laws in the 1970s, here in Missouri and in many other states, statutes have since been enacted which allow an individual to make a revocable transfer of real property, personal property or bank accounts and securities through a designation to a beneficiary in a real estate deed (a beneficiary deed), a bank account or security account (pay on death designation) or on a personal property title (transfer on death) which transfer avoids the probate proceeding without the necessity of a revocable living trust. In addition, the advent of the IRA and 401(k) plans in the United States since the 1970s has allowed for qualified plan proceeds to be transferred to surviving spouse's and others through a beneficiary designation form which also avoids a probate proceeding. Thus, there are tools available today which were not available when revocable living trusts were first introduced which may mitigate against the use of a revocable living trust in today's estate planning climate, at least with respect to married couples.

On several occasions I have had an opportunity to hear "estate planning experts" tell people that federal estate tax savings can only be achieved through the use of a revocable living trust as opposed to a will. That is categorically incorrect. You can obtain the same estate tax savings through the proper structure of a will as you can by using a revocable living trust. However, the fact of the matter is that where individuals have an estate that is large enough to incur federal estate tax (what ever that may be) the use of the revocable living trust to avoid the costs associated with probating the estate typically point towards the use of a revocable living trust as opposed to a standard will. I used to point to the $3.5 million estate tax exemption amount as the benchmark for setting up living trusts but given the fact that, at least for this year, there is no estate tax that benchmark is no longer really useful.

Now, the big problem with estate tax planning as a whole, at least currently, is that as of today there is no estate tax. This is because in 2002 Congress enacted estate tax legislation that repealed the estate tax beginning January 1, 2010, but only for one year. Beginning January 1, 2011, the new law expires and the "old" law, which imposed an estate tax of up to 55 percent on estates greater than $1,000,000, is back in effect. Most people expected Congress to act before the end of 2009, reversing the one year of repeal but do date That has not happened. Although this may sound like good news, it could be a real problem if your estate planning documents are not up to date. If you have questions about your current estate planning documents you should contact your attorney.

At this point I am sure many readers are wondering "well, why would I choose a standard will over a revocable living trust?". The basic reason is cost. Most attorneys charge double, triple or even more to prepare a revocable living trust then

they typically charge for preparing a standard will. This is typically because more legal drafting is involved and the attorney usually also advises as to the transfer of assets into the revocable living trusts which is necessary to achieve the probate avoidance. Depending upon the size of a couple's joint estate it may make more fiscal sense to go with standard wills at that point in their lives rather than pay a considerable amount more for revocable living trusts.