TO TRUST OR NOT TO TRUST

The Top 7 Reasons to Put Your Assets in Trusts

Richard Rubino, J.D. & Samuel J. Liang

· RUBINO & LIANG, LLC ·

There are many reasons why trusts have become so popular as an estate planning tool. Saving taxes is probably the most widely understood of these reasons. But at the end of the day there are other more personal issues which arise in people's lives that make trusts a useful tool when planning for the disposition of your assets. One of the more important of these is privacy. When you are placing property in trust and passing it to your loved ones in this manner, it is not a matter of public record and no one has to know what you are doing with your property. Another important issue is control. You can have provisions that make sure that assets stay in the control of your family – those no-blood-no-money rules. Trusts enable you to be very specific about who gets what and under what conditions. A trust is a very useful way to distribute your wealth to the people or charities you care about, and, it is perhaps the best approach for accuracy, specificity and avoidance of misinterpretation.

TWO TYPES OF TRUST

A trust is an agreement wherein a person formally transfers the title to his property to a trust, which is then managed for the beneficiaries named in the trust. In the first type of trust (revocable), the asset holder retains control of all the assets. In the second (irrevocable), the asset holder gives up control of the assets.

 © RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

TRUSTS CAN BE MADE EITHER REVOCABLE OR IRREVOCABLE BY YOU DURING YOUR LIFETIME

Both revocable and irrevocable trusts can be quite complex and the laws governing them are always changing, so creating one demands professional advice. In some circumstances you may want to utilize both revocable and irrevocable trusts. Any trust that is not drafted correctly could jeopardize disposition of the assets held by the trust.

Trusts are utilized for the purpose of transferring more asset value than a simple will would allow to your loved ones or charities. For this reason, trusts are designed to protect assets not just from probate, but from unreasonable taxation, creditors, spendthrift or wasteful children, greedy relatives, and nasty lawsuits your children might be involved in. Irrevocable trusts provide the highest degree of asset protection and can be thought of like a bullet-proof box to hold and manage your assets while you are alive as well as after your death.

1. A living or revocable trust (also called inter vivos, Latin for “within the living”) allows you to change or terminate the trust whenever you choose. Revocable trusts are used primarily to distribute assets directly to your beneficiaries without going through probate, but are subject to estate taxes if your property is over a certain amount since you essentially remain their owner. You can revoke the trust or remove any of the assets transferred into it at any time. You can even name yourself as the trustee.

2. An irrevocable trust cannot be changed or terminated, as the name implies. Since you’ve permanently transferred title to the property (of any amount) to the trust, there are tax and other benefits that are not available with a revocable trust. However, you do not have control of the assets and cannot remove them from the trust. In addition, transfers to an irrevocable trust are sometimes subject to gift tax rules. It is also important to select a trustee other than yourself to avoid problems with IRS.

*Estate Tax Credit is currently $1 million for the Commonwealth of Massachusetts and $5 million for the Federal Goverment (increased each year)

Trusts have been around at least since Roman times, but their clearest history is from the time of King Henry VIII in England. At that time, landowners were forced to pay fees to the crown and to serve in the military. To avoid that, they would try to hide their ownership of land by having someone else use it. King Henry was unhappy with these cheapskate draft dodgers, so he unwittingly defined the origins of modern trust law: full title of the land was automatically given to the person who was using it, which made the original owners quite distressed.

© RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

HERE ARE THE SEVEN MOST IMPORTANT PUBLIC REASONS FOR INCORPORATING TRUST PLANS INTO YOUR ESTATE DISTRIBUTION STRATEGY:

1. Avoid Probate

If you have written a will it will be subject to probate proceedings no matter how much or how little you have in your estate. Probate (from Latin probare, to prove) is a legal procedure that proves the validity of your will and oversees the distribution of your assets. It can cost a lot of money. Probate is not just costly, it can take an inordinate amount of time. Anywhere from six months to two years and counting. Probate is also open to the public, so your assets are open to public scrutiny.

The location of your assets (in terms of legal title) upon death determines how much money will be owed in taxed and fees. If your assets are held in your name (or your spouse's), they will likely be passed on through your will. A will, as we've learned, can be expensive in probate fees, but another option is to move your assets into a revocable trust, which automatically escapes probate.

Once the trust is set up, you put property and money into the trust during your lifetime for the benefit of yourself and possibly other family members. You can change or revoke the living trust at any time. You are both the creator of the trust and, while you are living, the beneficiary of the trust. You get to name yourself as the trustee to manage the assets. Alternatively the trustee can be a friend, a relative, or a bank. Typically in a revocable trust you are both the trustee and beneficiary and therefore you can remain in control.

To provide further peace of mind, a "pour-over" provision should be included in your will. It allows any assets not yet transferred to the trust (such as property acquired after the trust was created) to be poured over into the trust upon the death of the creator of the trust. You should also consider putting assets in the trust as you acquire them to avoid probate.

Now that you no longer own assets because they have been placed in the trust, they escape probate. And whereas, a will becomes effective only upon the death of the person who made it, a revocable trust is effective immediately. So you've saved time and money. Usually the only downside to a revocable trust is paying the lawyer to put it together.

 © RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

2. Transfer Property & Avoid Estate Taxes

What is the biggest tax event of your life? Your death. That's because no matter where you live in the U.S. at the time of your death, the portions of your estate that add up to over Federal and State limits are subject to estate tax. The IRS even assigns your estate a federal employer identification number (even though your estate is not an employer) just to keep track of it. Additionally, if you reside in Massachusetts, any amount over $1 million is also subject to state estate tax (kindly called the death tax by the state government) of up to 15%. Ouch.

Recall that a revocable trust allows you to change or terminate the trust whenever you choose. While assets in a revocable living trust pass directly to your beneficiaries without going through probate, they are subject to estate taxes if your property is over $1 million in Massachusetts since you essentially remain the owner and have control of the property.

Irrevocable trusts cannot be changed or terminated. Think of it as being carved in stone from the moment you create it. However, transfer to an irrevocable trust are subject to gift tax rules. You should also be aware that certain types of transfers to irrevocable trust that are made within 3 years of death are included in your taxable estate. Irrevocable trusts that include a life estate provision (where you retain possession or a right to income from the trust assets during your lifetime) remain in your taxable estate.

3. Reduce Estate Taxes Using a Credit Shelter Trust

The marital deduction allows you to pass assets to your surviving spouse free of estate taxes, deferring the estate tax rather than eliminating it. That's because your spouse's estate will have to pay the estate tax on the assets that remain at the time of his or her death. A credit shelter trust (CST) is a type of trust used by married couples to reduce estate taxes in this situation. Instead of giving all of your assets to your surviving spouse outright, you shelter a portion of your assets by putting an amount equal to the estate tax credit into the trust. Your surviving spouse cannot have unfettered access to the trust assets; otherwise, it would be included in his or her estate. The surviving spouse can have access to the income from the trust as well as a limited right to withdraw principal. At the time of the death of the second spouse, the remaining assets in the credit shelter trust go to the beneficiaries (usually the children) free from estate taxes.

A marital trust that is often used in conjunction with the credit shelter trust is the qualified terminable interest property trust, better known as the QTIP trust. Assets passed to the surviving spouse outside of the credit shelter trust are put in QTIP. The QTIP trust allows the creator to give lifetime benefits (like income earned on trust assets) to his spouse while still holding the right to name the persons (often his own children) to receive the trust assets upon his spouse's death. The QTIP trust qualifies for the estate tax marital deduction, which lets assets pass to the surviving spouse free of estate taxes, but is subject

© RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

to estate taxes on the spouse's death. The main purpose of the QTIP trust is not tax savings because it is used by the spouse, but rather to allow for asset control. It is useful if you have children from a prior marriage or are concerned that a spouse may not be able to manage assets in the future.

4. Wealth Replacement

Another popular trust is the irrevocable life insurance trust (ILIT). This type of trust avoids the hefty estate tax because it is irrevocable (it does not allow you to control the assets.) It is used to hold a life insurance policy and keep the proceeds from the policy out of your estate. There may be a gift tax liability when the trust is set up, but you will save a lot of money because the life insurance proceeds in the trust escape estate taxes and probate. To make sure the proceeds from the policy are not subject to estate taxes, you must not retain any "incidents of ownership" such as the power to change the beneficiaries, power to assign the policy, or ability to borrow against the policy. You pay the policy premiums by transferring money to the trust, and you can take advantage of the $14,000 annual gift tax exclusion. Initially, it is best to transfer some money to the trust, and have the trust purchase a new life insurance policy. You can transfer your existing policy into the trust but if you die within three years after you make the transfer, the proceeds from the policy will be subject to the estate tax.

An irrevocable life insurance trust is also sometimes referred to as a wealth replacement trust because it lets you pass on the proceeds of a life insurance policy separate from your estate, thereby avoiding estate taxes on the value of the payout upon your death.

5. Avoid Capital Gains & Benefit Charitable Interests

A charitable remainder trust (CRT) is used to make gifts to charity while still enjoying and earning income from the assets during your life. It actually provides for two groups of beneficiaries: 1) you and your spouse and 2) the charities you want to support. You and your spouse can continue to use the property and receive income from it while living. Upon your death, the charities receive the property. No capital gains tax will be due if the property is sold (because it is a charitable contribution and is thus tax-free.) Because the asset has been transferred by you from your estate, no estate taxes are due. You also get a charitable deduction on your income tax return in the year you transferred the assets into the CRT.

6. Protect Your Children From Their Own Bad Habits

A spendthrift clause is often added to either a revocable or an irrevocable trust that involves distributions to family members. It gives an independent trustee authority to make decisions as to how the trust funds may be distributed for the benefit of the beneficiary. The beneficiary – and any creditors – cannot reach the funds in the trust. It is called spendthrift because it often applies to a beneficiary who is a wasteful spender (like your yuppie playboy son), but it can also be used simply for basic asset protection from creditors. An incentive feature is often included in such a trust; you give more money to the beneficiary who improves his conduct (for instance if your playboy son becomes thriftier or decides to go to graduate school.) This clause allows you to limit spending of trust assets to worthy purposes like education, housing and medical expenses.

 © RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

7. Protect Your Assets When a Spouse Requires Nursing Home Care

Another use of an irrevocable trust is to protect assets if you or your spouse requires nursing home care. Medicaid is the means-tested government program that pays for nursing home expenses. If you exceed the Medicaid eligibility limits in savings and property, Medicaid will take the money and property away from you to pay for your care. Placing your assets in an irrevocable trust will make those assets inaccessible to Medicaid – and to anyone else for that matter, including yourself, so you have to be sure that this type of trust suits your needs.

One possible problem: Medicaid has a five-year look-back provision. Any transfer to a trust made within five years of your entering a nursing home will be counted toward the determination of your Medicaid eligibility. If you place assets in an irrevocable trust and you enter a nursing home within five-years, those assets will have to be paid to the nursing home. To avoid this outcome, the transfer should be made as soon as you can comfortably do it. Even if you do not set up this type of trust in time to avoid the look-back period, there are other last-minute planning techniques that can protect a portion of the assets. It is never too late.

We have provided you with explanations that should help you understand the reasons why trusts have become so widely used. Try not to get confused by all the names for trusts. In fact, the different types of trusts are usually made so by inserting the appropriate clause into a basic trust document. Self-interest is a fundamental part of economics; your estate is your own to distribute how you want, as intricately as you want. The goal of using a trust is to provide you with the tools you need to feel confident that you will be cared for during your life and that, after you pass away, your loved ones will share what you have worked so hard to create.

Sample Letter to Transfer Interest – *used to transfer assets into an existing trust*

ABC Company
Gentlemen:

Please be advised that I am currently the owner of ____________, account number. Title is presently held in the name of _________. I have recently created a ______ trust into which I have transfered the title to the above described item. The name of my _______ trust is _________.

If any other documentation is required to effect such a transfer, please notify me immediately. Otherwise, I will assume that all rights and ownership to such described item has been transfered by you to the ___________ [Name of your Live Trust]. Please confirm this transfer by return letter.

[Signature]

© RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

GLOSSARY OF TERMS

beneficiary: a person designated to receive payment from trust, will, or charitable remainder trust (CRT) that collects taxable annual payments from trust earnings or principal. At the donor's death, whatever remains of the trust principal goes to a charitable, religious, or educational institution

claim: right to payment from trust or will

creator, grantor, settlor: one who establishes a trust

credit shelter trust (CST): a trust that avoids state estate tax by preserving the $1 million estate tax credit of the first spouse to die

creditor: party with claim for payment, party you're indebted to

deduction: the act of deducting or subtracting from taxation. Sample estate tax deductions include donations to charity, funeral costs, and lawyer fees

estate: all property rights and interests owned and controlled by individual or trust

gift tax: federal tax on lifetime transfers of money or property not specifically excluded from tax by law

irrevocable trust: cannot be terminated or changed at any time

living trust: (also know as revocable trust) can be terminated or changed during life of the person who created it

marital deduction: a tax break that allows tax-free gifts of an unlimited amount to spouse

probate: (probate means surrogate, or taking the place of the deceased) court procedure that administers will. All property in will is subject to probate court proceedings and becomes knows as probate estate

property: anything you own, either tangible (jewelry, furniture, antiques, pets) or intangible (bank accounts, stocks, bonds)

spendthrift provision: clause in a trust that prohibits beneficiary's creditors from taking money from trust to satisfy debt

trustee: one who administers trust according to terms of trust document

will: legal statement that directs how property is to be distributed at death

Amounts given are valid as of this writing but subject to change by law

877.630.8787
189 Wells Avenue
Newton, MA 02459
www.JustDontLoseTheMoney.com

· RUBINO & LIANG, LLC ·

From your friends Rich & Sam...Protecting your wealth

© 2015 RUBINO & LIANG, LLC. ALL RIGHTS RESERVED

Rubino & Liang, LLC is not an affiliate or owned by any financial company. Insurance products are sold through R&L Insurance Agency, LLC. Professionals from Rubino &b Liang, LLC may transact business in states where properly qualified and licensed.