

REVOCABLE LIVING TRUSTS: MAKING THE RIGHT DECISION

BY RYAN M. WILSON

The revocable living trust is one of the oldest estate planning tools. Today, a revocable living trust is used for many reasons, including, but not limited to, federal estate tax savings, asset management and probate avoidance. However, is a revocable living trust right for you?

You may have heard your friend, co-worker or neighbor talking about her trust. You may have even felt left out without one for yourself. Just what is a trust? A trust is a legal arrangement or contract with respect to property in which a person (the “trustee”) holds title to property for the benefit of another person or persons (the “beneficiary” or “beneficiaries”). There are two different types of trusts, e.g., living and testamentary. A living trust can be either revocable or irrevocable. The one we are going to discuss is called a “revocable living trust” or “living trust” for short. This type of trust can be amended or revoked; however, the right to amend or revoke the trust terminates at death or incapacity.

The living trust is established by a written Trust Agreement. The Trust Agreement is between the person establishing the trust and the trustee. The person establishing the living trust is commonly called the “grantor” or “settler.” The Trust Agreement shows the intent to create a trust, identifies the grantor, the trustee, and the beneficiaries, and states the terms of the trust.

Despite the claims by many legal practitioners, a living trust is not appropriate in all circumstances. Whether or not a trust is appropriate for you will depend on many factors, including, but not limited to, the size of your estate, your goals and objectives, your family situation and marital status. A review of the advantages and disadvantages of a living trust will help guide our discussion.

Perhaps the biggest advantage of a living trust is the

ability to reduce or eliminate federal estate taxes for a married couple. By utilizing living trusts, a married couple can transfer up to \$4,000,000 without federal estate taxes for 2006-2008. Each person has a \$2,000,000 federal estate tax exclusion amount. By establishing a separate trust for the husband and wife, a couple can transfer a combined \$4,000,000 without federal estate taxes. If living trusts are not used, the surviving spouse is left with his or her own \$2,000,000 exclusion amount, and the exclusion amount for the deceased spouse may be lost. So, if you are married and have a federal gross estate in excess of \$2,000,000, living trusts may be right for you.

You do not have to have a large estate to justify the use of a living trust. There are many more advantages of a living trust. For example, a desire to provide for and protect someone is probably one of the most common reasons for creating a living trust. Although you could make a quick, convenient and uncomplicated outright gift, there are many situations in which such an outright gift would not effectuate your true intent. Minors lack legal capacity to manage property. A living trust permits the grantor to make a gift for the benefit of a minor without triggering the necessity for the minor to have a court-appointed conservator to manage that property.

An individual beneficiary may lack the skills necessary to properly manage the trust property as a result of mental or physical incompetence or lack of investment experience. By putting the money or property under the control of a trustee, you increase the likelihood that the beneficiary’s interest will be served for a longer period of time. You may also have a special needs child or grandchild. A living trust allows you to set up special needs provisions for your child or grandchild without affecting his or her governmental benefits and eligibility.

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REVOCABLE LIVING TRUSTS, continued

Under Michigan law, you may protect trust assets from the beneficiary's creditors by including a spendthrift provision in a living trust. A spendthrift provision does two things. First, it prohibits the beneficiary from selling, giving away or otherwise transferring the beneficiary's interest. Second, a spendthrift provision prevents the beneficiary's creditors from reaching the beneficiary's interest in the trust. It restricts the beneficiary's control over the property in any manner that you desire, as long as the restrictions are not illegal. This flexibility allows you to determine how the trustee distributes trust benefits. You can spread the benefits over time, give the trustee discretion to select who receives distributions and in what amounts, require the beneficiary to meet certain criteria to receive or continue to receive benefits, or limit the purpose for which trust property may be used, such as health care or education.

Quite often, a grantor wants to provide for a second spouse but wants trust property to pass ultimately to his own children from a prior marriage. A living trust is an excellent vehicle in these circumstances.

Perhaps the most popular reason for using a living trust is to avoid probate. Property in a living trust is not part of the probate estate upon the grantor's death. The property remaining in the trust when the grantor dies is administered and distributed according to the terms of the living trust; it does not pass under the grantor's will or by intestate succession. Generally, a living trust will accelerate asset management and distribution. However, the probate process in Michigan is relatively simple and not that expensive for a small estate.

Privacy is another advantage of a living trust. All probate proceedings are on the public record. Of course, the will itself is a public record. A living trust is usually not filed or recorded as a public record. Thus, a grantor can keep private the extent of his assets and their disposition.

If a decedent owns out-of-state real property, the decedent's will is usually probated in the state of the decedent's residence with some type of ancillary administration being necessary in the state in which the real property is located. This potentially expensive, inconvenient and time-consuming process may be avoided if the real property passes by way of a living trust.

A living trust can also be used to manage assets. You may create a living trust and maintain control over the trust property, for example, by serving as the trustee, retaining the power to revoke the trust and keeping a beneficiary life interest. However, upon your incompetency, your designated successor trustee would take over the administration of the trust property in accordance with the directions you expressed in the living trust. It can give you peace of mind knowing how your property will be managed.

A living trust is also very helpful for blended families and in second marriages. Quite often, a grantor wants to provide for a second spouse but wants trust property to pass ultimately to his own children from a prior marriage. A living trust is an excellent vehicle in these circumstances. A living trust may also preserve the unique nature of assets from a prior marriage. It may also be possible to disinherit a spouse by creating and funding a living trust; however, Michigan case law lends some uncertainty to this area. A living trust may be used to establish a marital deduction for a noncitizen spouse. And there are many legal practitioners who believe that a living trust reduces the risks of challenges to an estate plan, but this conclusion is debatable.

In summary, there are many advantages to using a living trust as part of one's estate plan, including the following:

- Reduce or eliminate federal estate taxes
- Provide for and protect beneficiaries
- Protect assets from beneficiaries' creditors
- Retain flexibility in disposition of estate
- Avoid probate
- Increase privacy
- Avoid ancillary probate of out-of-state real property
- Provide for asset management during lifetime
- Retain control for second marriages or blended families
- Obtain a marital deduction for a noncitizen spouse

Some of the commonly discussed disadvantages of living trusts include the additional costs to create the living trust, the necessity of funding the living trust, the requirement to monitor continually your assets and how they are owned, the severing of jointly held assets and the loss of certain creditor protections and the expanded statute of limitations in the event of a contest.

There is no easy "litmus test" to determine whether a living trust is the right decision for a client. Clearly, its usefulness has been overstated in many advertisements and seminars in which clients are told that they need a living trust to avoid probate. Some of the benefits of a living trust can

also be achieved through a well-drafted durable power of attorney, the election for unsupervised probate administration and/or the use of a will (possibly with testamentary trust provisions). Before a living trust is recommended to a client, the estate of the client, the status of the intended beneficiaries and the goals of the client must be considered. A living trust may be an extremely useful and effective part of a client's estate plan. However, living trusts are not appropriate in all cases. A careful review of the potential benefits and drawbacks must be made before deciding whether a client should include a living trust as part of the estate plan.



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ATTORNEY ACTIVITIES OF NOTE

■ Fraser Law Firm, with a team led by Jonathan Raven, won a hard-fought battle through the Court of Claims and the Court of Appeals. The win resulted in the implementation of a preliminary injunction against the State of Michigan arising out of a claim of breach of promise on behalf of a Michigan food distributor that had contracted with the State to deliver food commodities to school districts throughout the State.

■ Bob Nelson will speak at Michigan State University's Institute of Public Utilities "Regulatory Fundamentals for Utility Personnel and Analysts" on June 5 at the Kellogg Center. The topic will be video franchising.

■ Gary Rogers recently obtained very favorable results in three cases where he was representing defendants in lawsuits. In one case, the Plaintiff voluntarily dismissed his lawsuit after discovery was undertaken by Mr. Rogers regarding the alleged claim. In the second case, the Michigan Court of Appeals affirmed the trial court's dismissal of a personal injury lawsuit. The third case was a veterinarian malpractice lawsuit which was also dismissed by the Plaintiff after Mr. Rogers undertook discovery. None of the defendants in the above three cases paid anything toward settlement.

■ Fraser Law Firm has created a new Criminal Law Practice Group. Brian Morley will Chair the group. Mr. Morley is a member of the National Association of

Criminal Defense Lawyers and the Criminal Defense Association of Michigan

■ Iris Linder is a featured speaker in Research and Markets' "The Legal Side of Venture Capital Deals Seminar." The Seminar is available in audio CD and book format at www.researchandmarkets.com/reports/c36573. Ms. Linder's presentation is *Preparing for a Venture Transaction*.

GOLDEN NUGGET

Question: How does a living trust avoid probate?

Answer: The key in avoiding probate with a living trust is the retitling of assets. Assets titled in the name of the trust avoid probate. At the time of a person's death, if the asset is owned by the trust, it is not necessary to "probate" this asset in order to have control over the asset. The successor trustee of the living trust is able to control the asset as the trust agreement instructs. It is important to note that after a living trust has been created, it is necessary to transfer the ownership of assets held in the person's individual name over to the living trust during the person's lifetime, otherwise probate will not be avoided. Having a living trust alone does not avoid probate. You must take the second step of "funding" the living trust by transferring ownership of assets to the trust.

Interested in more information about Estate Planning and Probate issues? Sign up for Ryan Wilson's free monthly *Golden Bullets*. It is available in print and email format. For a subscription call Mr. Wilson at 517/377-0897 or email him at rwilson@fraserlawfirm.com.

MICHIGAN GAMING PUBLICATION ADDS REPORTER

The *Michigan Gaming Law Newsletter*, which is published by the Fraser Law Firm, added Lauren Jacobs to its editorial staff as a reporter. The *Newsletter* is a fax, e-mail and Internet based publication that reports on expansion and regulatory developments involving Michigan's casino, lottery, and horse racing industries. The *Newsletter* is in its 12th year of publication and is subscribed to by financial analysts, casino operators, suppliers, regulators, and city and state officials located throughout the world. The *Newsletter* is available to everyone at www.michigaming.com.



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