



LEGAL HOTLINE FOR TEXANS

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LIVING TRUSTS

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The Legal Hotline for Texans (LHT) is a telephone hotline providing free legal advice and consultation and other free legal services to Texans Age 60 and Older or Eligible for Medicare; Crime Victims Age 60 and Older and their Family Members and Authorized Claimants; and Pension and Retirement Plan Employees, Participants and Beneficiaries.

Eligible Clients can consult with an attorney of the Legal Hotline for Texans free of charge by calling one of the phone numbers listed above. If clients would like to consult with an attorney in their communities, or if ongoing representation by an attorney is needed, the Legal Hotline for Texans may be able to make a referral.

Depending on individual circumstances and local availability, such a referral may be to an organization providing free attorneys to low income persons, or may be to an attorney on the Legal Hotline for Texans' reduced-fee panel, or may be to a statewide or local lawyer referral service.

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THE LIVING TRUST IN ESTATE PLANNING

Many recent articles and do-it-yourself kits advocate the use of a living trust as a way to avoid the probate of a person's estate. These articles are often aimed at seniors who are concerned about the potential high cost to their family of transferring their assets upon their death. This pamphlet answers some questions about the living trust and the advantages and disadvantages of its use.

Q: What is meant by "Living Trust"?

A: The term "living trust" refers to an arrangement that is created during the lifetime of the "grantor," or person setting up the trust, whereby the grantor transfers all of his or her property to a trustee pursuant to a written trust agreement. This agreement typically provides for the trustee to distribute all of the income from the trust to the grantor during his life (the income beneficiary), and designates the beneficiaries of the assets of the trust upon the death of the grantor (the remainder beneficiaries). In the typical agreement, the grantor is named as the trustee and the trust is "revocable," meaning that the grantor has the right to amend or revoke the trust at any time. Upon the death of the grantor, the terms of the trust cannot be changed.

Q: What are the advantages of a Living Trust?

A: The living trust has certain advantages, primarily for *large estates* in which management of the assets, income tax planning and privacy are important considerations. A grantor using a revocable living trust can shift the responsibility of investment decisions to an appointed individual or bank trustee who could provide uninterrupted management of the trust assets upon the grantor's death. In addition, the trustee could have the power to distribute trust income to several beneficiaries in order to spread the income and resulting income taxes among several beneficiaries, thereby reducing the income tax liability of the grantor during his or her life. Otherwise, all of the income in the typical trust is distributed to and taxable to the grantor. Another advantage of a living trust is that upon the death of the grantor, the assets in the trust would not be listed in the publicly-filed inventory and appraisal of the grantor's estate; this is desirable where the grantor has a need to maintain privacy regarding his or her investments or beneficiaries.

Q: How does a Living Trust affect probate?

A: A living trust *can* reduce or eliminate the costs of probate but this should *not* be a controlling reason for creating a revocable living trust. Any probate cost savings must be offset by the costs of setting up and administering the trust during the lifetime of the grantor.

Q: Are there expenses to setting up a Living Trust?

A: Yes. The grantor will incur legal expenses upon the creation and maintenance of a living trust. We recommend that a lawyer draft the trust agreement according to the specific wishes of the grantor regarding the distribution of income and principal and the ultimate beneficiaries and according to state laws; a lawyer should also assist in reviewing the assets of the grantor to determine which assets are appropriate trust assets. Finally, a lawyer should prepare the necessary documents to transfer real property, such as the homestead, into the trust by an appropriate deed. Any life insurance on the life of the grantor should be considered so that the beneficiary designations are consistent with the client's total estate plan. Further, the grantor still needs to have a valid will that disposes of property not included in the living trust, such as automobiles and personal property. Any person considering the use of a living trust should compare the current expense of setting up the trust as well as the ongoing expense of administering the trust with the *future one-time-only* expense of probate which will be incurred by his or her heirs. For the person who already has a valid will that contains his or her estate planning wishes, the additional expenses of a living trust may be unnecessary.

Q: Can't I just buy a "kit" and set up my own Living Trust?

A: Some people want to know if they can set up the trust and manage it themselves by the use of a mail-order "kit" which they have seen advertised. This would be just as inadvisable as a person prescribing his or her own medications or pulling his or her own teeth. A lawyer should prepare the trust agreement and deeds. The "kits" available through mail order contain very general forms that may not be appropriate to Texas law, or to a person's individual wishes. It has been observed by lawyers that mistakes made by non-lawyers in the drafting of legal documents can result in legal fees that *greatly exceed* that which would have been paid to a lawyer to prepare the documents in the first place.

Q: What are some of the disadvantages of a Living Trust?

A: The costs of setting up the trust are one of several possible disadvantages to the use of a living trust. Other costs of the trust may include trustee fees if a bank trustee or other independent trustee is named by the grantor. Trustee fees could be a yearly charge based on a percentage of the principal of the trust. There could also be additional tax preparation fees. If the trust has income beneficiaries other than the grantor (where one of the purposes of the trust is to spread the income among several beneficiaries), the trust must obtain a separate tax identification number, and the trust will incur the expense of filing yearly income tax returns and K-1 forms (reports of income distributed) for each beneficiary. If the grantor is the sole beneficiary of the trust, the IRS does *not* require the trust to have a separate identification number and the trust accounts can be set up with the grantor's social security number.

Q: Can a trust be established for a developmentally disabled person, which the State cannot seize or invade to pay for services?

A: Yes, but this only applies to a resident admitted to a residential care facility, and then only if the trust has an aggregate principal of \$250,000 or less. The Texas Health and Safety Code, § 593.081. Trust Exemption provides:

(a) If the resident is the beneficiary of a trust that has an aggregate principal of \$250,000 or less, the corpus or income of the trust for the purposes of this subchapter is not considered to be the property of the resident or the resident's estate, and is not liable for the resident's support, maintenance, and treatment regardless of the resident's age.

(b) To qualify for the exemption provided by Subsection (a), the trust must be created by a written instrument, and a copy of the trust instrument must be provided to the department.

(c) A trustee of the trust shall, on the department's request, provide to the department a current financial statement that shows the value of the trust estate.

(d) The department may petition a district court to order the trustee to provide a current financial statement if the trustee does not provide the statement before the 31st day after the date on which the department makes the request. The court shall hold a hearing on the department's petition not later than the 45th day after the date on which the petition is filed. The court shall order the trustee to provide to the department a current financial statement if the court finds that the trustee has failed to provide the statement.

(e) Failure of the trustee to comply with the court's order is punishable by contempt.

(f) For the purposes of this section, the following are not considered to be trusts and are not entitled to the exemption provided by this section:

1. A guardianship established under the Texas Probate Code;
2. a trust established under Chapter 142, Property Code;
3. a facility custodial account established under Section 551.003;
4. the provisions of a divorce decree or other court order relating to child support obligations;
5. an administration of a decedent's estate; or
6. an arrangement in which funds are held in the registry or by the clerk of a court.

Source: §593.081, Texas Health and Safety Code (2001); 42 USC 1396p(d)(4) Trusts.

Q: Won't probate cost my heirs a lot of money?

A: Not necessarily. A common misconception relates to legal fees charged for the probate of an estate. Most heirs can obtain legal counsel to handle an uncontested probate of an estate on a set fee basis rather than a "percentage of the estate" basis. This is especially true when a decedent left a valid will and where an abbreviated probate procedure can be used. The family should be selective in choosing an attorney and should always discuss the fee arrangement with the lawyer prior to engaging his or her services. In a typical small estate, a valid will is the best and least expensive tool to transfer property at death.

Texas residents should be aware of the many favorable probate laws that can greatly reduce probate expenses. A properly drafted will can appoint an Independent Executor that will allow the estate to be managed with minimal court involvement. A Texas will can be "self-proved" by use of an affidavit that is signed by the witnesses to the will; this can expedite the court procedure where the will is presented. In Texas, many estates can be handled by an abbreviated probate procedure in which the will is probated as a "Muniment of Title". This procedure can be used when all of the debts of the decedent have been paid (except those secured by liens on real estate) and the court finds there is no necessity of administration. A probate of a will as a muniment of title avoids the necessity of filing an inventory and appraisal or of having an executor appointed. This procedure is very useful where the estate consists mainly of the deceased's homestead and automobiles of the deceased.

Q: How can I provide for a simple transfer of all my property to my husband or wife upon my death?

A: Many married persons would like for all of their jointly-owned property to transfer to their spouse upon their death. Most jointly-owned bank accounts are set up as joint accounts with "right of survivorship." Such an account will automatically become the property of the survivor upon proper proof that one joint owner is deceased. It is now possible for spouses to create this right of survivorship in all of their jointly-owned property. This can be done by a simple written agreement between the spouses called a "Survivorship Agreement," which will allow for property described therein to vest in the surviving spouse as a non-testamentary transfer. The [Texas Probate Code § 451](#) (and the sections following) deal specifically with this agreement and its requirements. It is crucial to understand that this agreement only applies to spouses and would not have any effect on the ultimate disposition of the marital property at the death of the second spouse. In other words, a person who has a "Survivorship Agreement" also needs a valid will. Of course, a person's home retains its status as "exempt property" as long as it is being used as his or her homestead.

Q: What issues would a Living Trust *not* address?

A: It should be noted that the living trust has no effect on certain financial matters. The existence of a revocable living trust will not affect estate taxes since the trust assets will be included in the grantor's estate. (No federal estate taxes or Texas inheritance taxes are levied on estates valued at less than \$1.5 million in 2004-05. This exemption will increase to \$2 million for 2006-08 and to \$3.5 million for 2009.). Additionally, a person can continue to be eligible for the "over 65" (includes age 65) exemption for ad valorem taxes on a personal homestead even if the homestead is transferred to the trust, so long as the person seeking the exemption is living in the homestead. The revocable living trust will also have no effect on any claims by creditors against the grantor's property -- since the grantor has the power to revoke the trust, creditors can attach living trust assets which are not otherwise exempt.

In summary, the Revocable Living Trust is a useful estate planning tool in certain circumstances; however, a person considering its use should discuss his or her personal financial situation with a lawyer who is competent in estate planning.