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Family Law & Estate Planning newsletter

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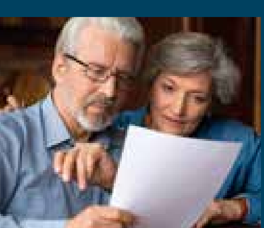

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So You Think You Need a Revocable Trust?

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PREPARING FOR YOUR ESTATE PLANNING APPOINTMENT

Estate planning is a crucial aspect of financial management that often gets overlooked until it's too late (nobody likes to think about their own mortality). It involves creating a plan for the management and distribution of your wealth during your lifetime and after your death. Proper estate planning also ensures that your loved ones are taken care of and that your wishes will be respected when you are no longer able to manage your affairs. To that end, a good estate plan starts with you, the client. In preparing for your estate planning appointment, it is important to take an inventory of your assets and give prior, thoughtful consideration to whom you want to administer your estate, how your assets should be distributed, and any family issues that may require specialized planning.

Take Inventory of Your Assets

It is hard to know where you are going if you don't know where you and your family are at financially. Therefore, your first step in the estate planning process is to complete an inventory of your assets and debts. Start by making a comprehensive list of all

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your assets, including real estate, investments, bank accounts, retirement accounts, life insurance policies, and personal property. If you're married, be sure to separately itemize your spouse's assets and debts. Each item should be listed at its current fair market value. Joint accounts and other co-owned assets should be noted as such with the appropriate adjustment to reflect your proportionate share of the asset's value.

Before the initial appointment, your attorney will likely have you complete an estate planning questionnaire that includes a financial inventory. It is important to provide supporting documents where possible, such as real estate deeds, financial statements, and life insurance policies. Your attorney may need the information on these records to implement your estate plan. Remember that your attorney will be relying on the information you provide when advising you about different planning options. If the information is inaccurate or incomplete, his or her recommendations and your documents may not be appropriate.

Clearly Define Your Values and Goals

The next step is to clarify your values and goals. What do you want to accomplish with your estate plan? Do you want to provide for your loved ones, minimize taxes, or support a charitable cause? Does gifting property during your life make sense or will that money be needed during retirement? And what does retirement look like for you? For some people, retirement means relocating somewhere warm. For others, retirement might involve transitioning to a limited role in a family business. Defining your objectives will help you make informed decisions throughout the estate planning process and ensure that your plan aligns with your values and goals.

Choose Trusted Personal Representatives, Trustees, and Other Fiduciaries

One of the most difficult choices you will make during the estate planning process is who to appoint as your fiduciaries. Fiduciaries, in the estate planning context, include personal representatives that will administer your estate, trustees to manage your inter-vivos or testamentary trust[1], and agents to act under a durable power of attorney and a health care directive. By default, most people will select their spouse as the primary fiduciary with one or more children serving as the back-up or successors; provided, however, that you will almost always serve as the initial trustee of your revocable trust.

While these default fiduciaries work well in the majority of cases, every situation is unique and you should still give careful consideration to the suitability of your proposed candidates. Ask yourself the following questions:

- What knowledge, skills, and experience does your proposed candidate possess? At a minimum, your fiduciary should be reliable, honest, and fiscally responsible. Although large and complex estates might benefit from a more sophisticated fiduciary, he or she can hire accounting, investment, and legal professionals as needed.

- What are the attitudes and philosophies of your candidate? How does the candidate understand their duty to manage your estate? Is that understanding consistent with your goals? For example, trustees often have discretion in how they administer a trust. The trustee's investment strategy and plan for retention or liquidation of assets (such as a family farm or closely-held business) should align with your broader estate planning goals.

- How will family dynamics impact the administration of your estate? Your children might have a good relationship today, but things could turn ugly if one of your children is forced to deny an unreasonable distribution request from their siblings or your surviving spouse.

- Are there any potential conflicts of interest that should be avoided? In general, a fiduciary should avoid transactions that benefit them personally over other interested persons. The fiduciary should not engage in transactions that involve the fiduciary, the fiduciary's spouse, or an entity controlled by either. Any contract or transaction affected by a conflict of interest should be expressly authorized in the terms of your estate plan. For instance, you could authorize your trustee to rent the trust's farmland to himself at fair market value or a discounted rate. It should also be noted that Minnesota's Trust Code generally prohibits trustees from making discretionary distributions to themselves, as a beneficiary, unless the power to make a distribution is limited by an "ascertainable standard" such as health, education, maintenance, and support.

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[1] An inter-vivos trust is a type of trust created during your lifetime. It can be revocable or irrevocable. A testamentary trust is a trust that is established after death under the terms of your last will and testament.

Professional fiduciaries, including certain banks and trust companies, offer another alternative to individual fiduciaries. Having a truly independent trustee is advisable when there is a risk that separate factions within the family will be vying for control of your estate. Tax considerations may also require the use of an independent fiduciary.

Determine How You Would Like Your Assets to be Distributed

Consider the dispositive plan you would want if there were no taxes to avoid. Your plan should be an extension of your pocketbook and your property should be used in the same well-reasoned ways that you would employ if still alive. Avoiding taxes isn't going to make you happy if the overall estate plan isn't what you really want.

The traditional plan will give all assets to your surviving spouse or, if none, to your children in equal shares. A gift of your entire estate to the surviving spouse will have the practical effect of delaying your children's enjoyment of their inheritance. This tradeoff makes sense because most people want to ensure their spouse is provided for later in life.

Assuming that you have a spouse, you will need to decide whether the spouse's share of your estate is distributed outright or held in further trust. An outright distribution is the simplest approach and often preferred by the spouse. Your spouse will have complete control over the assets, but those assets will be subject to claims from the spouse's creditors.

Alternatively, you could choose to place your spouse's share of the estate into a special marital trust known as a Qualified Terminable Interest Trust ("QTIP Trust"). A QTIP Trust is attractive for individuals that want to retain a degree of control over their assets after death. These trusts are sometimes used in situations where the decedent had children from a prior marriage. The QTIP Trust will pay out net income to the surviving spouse each year for life. After the spouse's death, the trust will terminate and be distributed to the beneficiaries designated by the decedent. And the underlying assets within the QTIP Trust are sheltered from the spouse's creditors.

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Regarding children and more remote descendants, your estate plan should make sense whether you live ten years from now or die tomorrow. Do you have minor children? Are you concerned about one of your children getting divorced? Does a child suffer from addiction? Give careful thought to the age, maturity, and disability of your descendants. It may be advisable to place your child's share into a sub-trust with restrictions on distributions for specific purposes or until a child reaches a suitable age. Many children under the age of 25 would act irresponsibly if they received a large inheritance outright and free of trust.

Plan for Incapacity

Incapacity can happen unexpectedly due to illness, accident, or age-related decline. Your estate plan should also include provisions for the management of your estate and your physical person during periods of incapacity. These documents may include a durable power of attorney for financial matters and a health care directive for medical decisions. Additionally, if your assets are held in a revocable trust, the successor trustee will usually continue spending trust assets for your support and benefit. Depending on the nature of the disability, a more restrictive guardianship or conservatorship could be avoided.

Conclusion

While you don't need to figure everything out on your own, it is important to clearly identify your values, what you own, and your legacy goals before beginning the estate planning process. This will help you and your attorney create an estate plan that is accurate, flexible, and no more complex than is needed for your circumstances. The information provided in this article is not intended to and does not constitute legal advice. The statements herein are for general informational purposes only. Should you have a question about your specific situation, it is recommended that you consult with a licensed attorney or other professional.

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DIVORCE AND YOUR ESTATE PLAN

The last thing a person wants to do after getting divorced is spend more time with a lawyer. But updating an estate plan after divorce is crucial. In Minnesota, when a dissolution is granted a former spouse's interest in the ex-spouse's will is terminated as if the ex-spouse had died one day prior to the Judge signing the divorce decree. This also applies to revocable living trusts: any interest or ability that an ex-spouse has to manage the revocable living trust is terminated as if he or she had died.

However, this only applies to a former spouse, not anyone else. For example, if a will grants "one-half to my wife's heirs-at-law" the former wife's heirs still have a one-half interest in the estate. This is precisely the outcome of *In the Matter of the Estate of Matthew Joseph Tomczik*. While the couple did not have children, Tomczik's ex parents-in-law received half of his estate upon his death. This case is currently being reviewed by the Minnesota Supreme Court but for now this is a precedential opinion that judges in Minnesota must follow.

It is important to note that Minnesota is unique. Minnesota has adopted much of the Uniform Probate Code, such as the provision which revokes devises to a former spouse, but not all of it. In 1990 the Uniform Probate Code expanded the devise revocation to a former spouse to also include revoking devises to relatives of former spouses. Minnesota has not adopted this part of the Uniform Probate Code.

Beyond testamentary documents, a divorce has other far flung financial ramifications. In another recent case, a Minnesota man's ex-wife died in 2019 and he sought her 401(k) worth $600,000.00. Their marital termination agreement, signed in 2002, granted wife all right, title, and interest to her 401(k); however, she never changed him as the listed beneficiary on the account. The district court originally ruled that the 2002 agreement was ambiguous and did not state clearly whether it was wife's intent that her husband be a beneficiary of the account. This is now back in front of the district court for further review. Clearly expressing your intent across all of your affairs is necessary to protect your intentions and your heirs interests.

It is also important to revisit any power of attorney decisions. In Minnesota, an otherwise valid power of attorney is automatically terminated if the power is granted to a spouse and proceedings commence for dissolution, legal separation, or annulment of marriage. Again, it is important to note that this only applies to spouses, not other family members. For example, if a spouse has power of attorney for an elderly family member it will not automatically terminate when the divorce process begins.

As with any legal document, an estate plan's language is crucial. It is critically important to update an estate plan after any large life event, especially a divorce. But simply updating your will isn't enough to safeguard your estate. You must take action across all of your accounts and interests to protect your estate, and the people you want to benefit.

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SO YOU THINK YOU NEED A REVOCABLE TRUST?

It is a common conception today that a revocable trust is the "one-size fits all" solution to all estate planning needs. While a revocable trust is a powerful tool in building an estate plan, it is not necessarily the right tool for all. This article will discuss the factors you should consider when determining whether a revocable trust is right for you.

What is a revocable trust?

A trust is a separate legal entity that holds property for the benefit of others. The person who creates and funds the trust is known as the settlor (sometimes referred as a grantor or trustor). The person who is responsible for carrying out the terms of the trust and managing its assets is known as a trustee. Anyone who has the right to receive assets or income from the trust is known as a beneficiary. The settlor dictates through the trust document how the assets and income are distributed from the trust. A trust is typically created when the settlor executes a written declaration establishing the trust and transfers property to the trustee for the benefit of the trust's beneficiaries. However, a valid trust may be established without formally funding the trust with assets. Obviously, funding the trust is a critical step in establishing the trust and should not be unnecessarily postponed.

A revocable trust is a specific type of trust that is created by the settlor during their life. The settlor can alter, amend, or revoke the trust in its entirety. The settlor can also add or remove property as he or she deems appropriate. These retained rights of control and beneficial enjoyment cause the trust to be treated as a revocable trust under law. Once the grantor passes away, the trust document will dictate how the trust assets are to be administered. Those assets might be held in further trust or distributed outright to the settlor's beneficiaries.

What are the benefits of a revocable trust?

There are two main advantages to establishing a revocable trust. The first is that a revocable trust is highly effective in transferring assets such that much if not all of an estate's assets can avoid the probate process. With a revocable trust, the trust continues after the death of the settlor and the successor trustee can automatically transfer the trust assets to the designated beneficiaries. Since the settlor did not own the trust assets at the time of passing, they are not considered part of the probate estate. Avoiding the probate process is desirable because it simplifies the process by which the settlor's beneficiaries receive their assets, preserves the privacy of the estate by avoiding the public disclosure of the estate's assets, and, to the extent real estate is held in trust, avoids the need to commence multiple probate actions in other states where the real estate may be located.

The second advantage of a revocable trust, and the advantage that sets it apart from other estate planning tools, is that it affords the settlor the most amount of control over the assets in the trust. A revocable trust may be revoked by the settlor at any time and for any reason. The settlor can also add or remove assets, and change the trust's beneficiaries at any time. This means that, even though the settlor does not directly own the assets held by the trust, the settlor still maintains a level of control over the assets that the settlor would have if he or she owned the assets individually. In these ways, a revocable trust gives the settlor the most flexibility to respond to unforeseen circumstances and adjust their estate plan if necessary.

What are the drawbacks and limitations of a Revocable trust?

While all of these benefits can make a revocable trust the best option for some people, there are other considerations that you should make when determining if a revocable trust is the best option for you. First, because revocable trusts give the settlor a high level of control over the assets in the trust, revocable trusts are considered tax neutral, and any income generated by the trust's assets are considered income of the settlor for tax purposes. Similarly, the assets in the trust would be considered assets of the settlor for estate tax purposes. Therefore, if the total value of your taxable estate at death exceed the Minnesota estate tax exemption, $3 Million at the time of writing, a revocable trust by itself may not be the best option for you because it would have no effect on the estate tax liability faced by your estate. Second, assets held in a revocable trust are not beyond the reach of creditors and therefore creditors may recover from the assets of your revocable trust in collection actions. This includes nursing homes and medical assistance programs. Third, a trustee has a fiduciary duty to the trust's beneficiaries. Broadly, this means that the trustee has a legal duty to act in the best interest of all the beneficiaries when managing the trust and its assets. The trustee has a duty to account for their actions and to keep beneficiaries reasonably informed of the trust's administration. These duties don't strictly apply to a settlor of a revocable trust, but would apply to any co-trustee or successor trustee.

Alternatives to a Revocable Trust.

There are a wide array of options available in the estate planning toolkit that can accomplish probate avoidance while also addressing the limitations associated with revocable living trusts such as tax neutrality, creditor claims, and complicated fiduciary duties.

The alternative most similar to a revocable trust is an irrevocable trust. Irrevocable trusts accomplish most if not all of the probate avoidance of a revocable trust, but because an irrevocable trust cannot be revoked by the settlor, it is considered an entirely separate entity for tax and liability purposes. This means that the assets held in a properly drafted irrevocable trust will not be considered assets of the settlor's estate for estate tax purposes (although the transfer could constitute a taxable gift for gift tax purposes). An irrevocable trust can also protect the assets held in the trust from creditor claims or lawsuits. However, in order to enjoy the above benefits, an irrevocable trust must be specifically drafted to comply with applicable laws and requirements. Additionally, since an irrevocable trust may not be revoked or modified by the settlor after its creation, it is important to ensure that the trust is set up correctly and represents the settlor's wishes in perpetuity.

If your estate is small enough or the mix of assets is not overly complex, you may be able to avoid probate without a trust. For example, bank accounts, individual retirement accounts, stock and other securities, and life insurance policies usually allow the owner to designate a beneficiary to receive the assets on death of the owner. Real estate, motor vehicles, and many other assets can be titled in joint ownership with the right of survivorship. These assets will transfer to the designated persons without having to commence a probate action.

Real estate and other business assets can also be transferred to a business entity, such as a limited liability company or limited liability partnership. LLCs and LLPs can function to avoid probate because the entity will typically continue in existence after the death of the shareholder or partner.[1] They also provide a middle ground between revocable and irrevocable trusts in terms of the level of asset control provided to the estate planner. However, these business entities are governed by a different area of law and therefore would require different documents in order to effectively distribute the assets in accordance with your larger estate plan.

Conclusion

A revocable trust may be one of the first things that comes to mind when thinking about estate planning, however it is not the one size fits all solution that some consider it to be. While there are significant benefits to including a revocable trust in your estate plan, there could be more advantageous alternatives that better suit your needs. Sorting through these options and planning your estate may seem daunting, but making these considerations ahead of time can make a tremendous difference to you and your loved ones and there are many attorneys experienced in estate planning to assist in creating the right estate plan for you.

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[1] The underlying ownership interest (stock, partnership unit, etc.) is an independent asset that comprises part of your estate. To avoid probate, the ownership interest would need to be transferred to a trust or registered with transfer on death designation in compliance with Minnesota law.

Estate Planning Services

Estate Planning is important to ensure the orderly transfer of family assets, as well as to protect those assets from unnecessary taxation. The Gislason & Hunter Estate Planning Practice Group offers a variety of services to assist you in creating the best plan for you, your family, your business or your farm.

Some of the many services our attorneys offer include the following:

- Drafting wills, trusts, codicils and powers of attorney
- Preparing health care directives and living wills
- Creating family business succession plans with emphasis on each family's particular goals and values
- Farm estate and succession planning
- Evaluating estate and gift tax issues and structuring planning options to minimize tax obligations
- Administering and assisting clients with probate proceedings, conservatorships and guardianships
- Advising on Medicaid, Medicare, nursing home and elder law issues
- Handling disputed estate and probate matters in litigation, arbitration or mediation formats

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Your family's legal issues are unique. At Gislason & Hunter, we strive to develop customized strategies for your family's particular legal needs and will help you prioritize your goals to efficiently achieve a favorable outcome. You will receive the full range of legal experience and expertise offered by a large, full-service law firm along with individualized attention to guide you through what for most is the most difficult time of your life and move your life forward.

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