

What Is a Revocable Trust, and Should You Have One?

By Abbe I. Herbst

I'd like to have a living trust," is a request that I often receive from clients and potential clients. The purpose of this article is to explain the mechanics of a so-called living trust or revocable trust and to discuss the pros and cons of revocable trusts.

Trust Basics

A trust can be established by a trust agreement, intended to be effective immediately. It is a written agreement, entered into by the creator, who is commonly called the "grantor" or "settlor," and a trustee who has the duty to invest and administer the assets in accordance with the terms of the trust agreement. The trustee can be an individual or a bank or trust company, or a combination. Sometimes, the grantor can be the sole trustee.

If the terms of the trust can be amended, or even revoked entirely, the trust is known as a revocable trust.

The terms of a trust can also be set forth in a will, which becomes effective upon death, in which case it is referred to as a testamentary trust. This article will discuss only revocable trusts. Because a revocable trust is created by an agreement between a grantor and one or more trustees, it is sometimes known as a living trust.

A trust is a legal entity, and so if the trustee is to be responsible for the trust's assets, they must be registered in the name of the trust. This means, for example, that the legal ownership of bank accounts and stocks and bonds must be in the name of the trust, ownership of tangible personal property has to be re-titled or assigned to the trust, deeds to real property must be prepared and recorded showing the trust as the owner, and the consent of a cooperative apartment corporation board of directors must be obtained for the stock

of a cooperative apartment and the proprietary lease to be re-registered in the name of the trust.

A typical revocable trust agreement provides that the assets held by the trustee in the trust are to be managed for the grantor's benefit during the grantor's lifetime. In most cases, the grantor retains certain rights over the trust assets during his or her lifetime, such as the rights to receive the income of the trust, to withdraw all or some of the principal of the trust, to instruct that charitable gifts or gifts to individuals be made from the trust, as well as the right to amend or revoke the trust. It will also include instructions for how the trust assets are to be distributed following the death of the grantor, just as a will would do. Indeed, sometimes a revocable trust is intended as a will substitute.

The trustee's responsibilities include the safeguarding of the assets in the trust, the prudent investment of the assets, following the dictates of the trust agreement, and making payments to or for the benefit of the grantor or to others as the grantor may direct. Very often, when the grantor serves as a co-trustee with someone else, the grantor alone will have all the trustee's responsibilities and the other co-trustee serves as a stand-by trustee if the grantor should become incapable of serving, die, or voluntarily relinquish the duties of a trustee, thereby ensuring continuity of management.

Advantages of Revocable Trusts

One of the most significant benefits of a revocable trust is the continuity of management secured by having a trustee or co-trustee in place who is ready to step in and assume management of the trust assets if the grantor becomes unable to do so. If assets are in an individual's name, this continuity of management is also available through a durable general power of attorney. Sometimes, however, the





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power of attorney document cannot be located when the need arises, or delays may be caused by the legal or compliance divisions of banks, brokers and transfer agents in giving effect to the power of attorney.

Another advantage of revocable trusts is the relative ease of making changes, typically requiring only a signed and notarized writing, delivered to the trustee. Changing a will, on the other hand, requires witnesses and a notary public.

More stringent requirements attach to enforcing a will than to a revocable trust. For example, a will must be admitted to probate by a probate court before it can be given effect, there are sometimes delays before a will is admitted to probate, certain family members must be given notice of the probate proceeding and the opportunity to contest the probate of the will, and the will itself is a public record. A revocable trust, on the other hand, does not need court involvement to become effective (although its terms can be contested if someone brings an action) and is not a public record.

Disadvantages of Revocable Trusts

As explained earlier, in order to be part of a revocable trust, assets must be re-registered in the name of the trust. Depending on the nature of the assets, the process may be time consuming, cumbersome, and may involve additional costs such as satisfying a mortgage or paying recording fees.

The grantor may not want a co-trustee to know about all of the grantor's financial affairs, and so there is some loss of privacy.

In addition, the trustee of a revocable trust may be entitled to compensation for services as trustee. If, instead, the assets are in an individual's name until death, there is no such compensation payable until after the will has been admitted to probate.

Misconceptions About Revocable Trusts

There are many misconceptions about revocable trusts. One is that they can save taxes. This is a myth. Revocable trusts do not save income taxes or estate taxes.

Nor do revocable trusts protect assets from the reach of the grantor's creditors. Because the grantor can revoke the trust, its assets may be subject to the claims of the grantor's creditors.

It is not true that the terms of a revocable trust cannot be challenged by disappointed heirs or beneficiaries. They might not receive notice, as they do in probate proceedings, but trust contests are possible. In New York and elsewhere, the testamentary capacity needed to be able to execute a will is an easier standard to meet than the contractual capacity needed to be able to execute a trust agreement. In other words, it may be easier to void a revocable trust than a will.

Conclusion

Revocable trusts are not appropriate for everyone. Each situation is unique, and depends on many factors, including an individual's needs and concerns, the nature of his or her assets, and the willingness of the owner of the assets to take all the steps needed to transfer the assets to the trust. ▲

