Trusts 101

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VII. TRUSTS 101

A. Types, Goals, and Functions of Trusts

When created: A Trust created during the Trustor's lifetime is an *inter vivos* Trust. A Trust created after the Trustor's death is a testamentary Trust.[1] For example, a testator could execute a Will leaving his assets to his children, but create the condition that the children are age 21 before taking their share. When the testator dies leaving children under age 21, a testamentary Trust is created by the Will, lasting only until the children reach age 21.

The purpose of any Trust is to serve the Trustor's intent.[2] Settlors can have a wide variety of reasons for creating a Trust, therefore there are many types of Trusts, especially in the estate planning context.

Living Revocable Trusts

The most common estate planning Trust is the Living Revocable Trust. Most people use a Living Revocable Trust to avoid the need for probate after death. Due to the testamentary nature of these instruments, Living Revocable Trusts are Will substitutes and must be executed with the same formalities of a Will. The Florida Trust Code Section 736.0403(b) governs the formalities for creating a Trust which have "testamentary aspects," meaning the instrument disposes of the Trustor's property at his death, other than to the Trustor's estate. Although Living Revocable Trusts are Will substitutes, a "Pour-Over Will" should still be used to ensure all of the testator's assets make it to the Trust.

A typical Living Revocable Trust is one created by one or two people, typically a married couple, who are the Trustees and sole beneficiaries during their lives. They retitle their assets to

[1] Florida Statute §736.0401
[2] *Watson v. St. Petersburg Bank and Trust Company*, 146 So. 2d 383 (Fla. 2d D.C.A. 1962)

the Trust but still use and spend the Trust assets just as freely they did before having a Trust, and can change the Trust by agreement of both Trustors. In the case of a single Trustor, the Trust becomes irrevocable at the Trustor's death. At that time, the named successor Trustee takes legal title to the Trust assets and must distribute them to the beneficiaries as the Trust directs. In the case of a married couple who create a Trust, after the death of one Trustor, the surviving Trustor is the sole beneficiary. The survivor usually has the power to change the Trust terms, change the Trust beneficiaries, or even terminate the Trust. I will discuss Living Revocable Trusts further in Part IX of this presentation.

GRAT (Grantor-Retained Annuity Trust); GRUT (Grantor-Retained Uni-Trust)

When someone with a large estate makes a substantial gift, a GRAT Trust or a GRUT Trust can be established to minimize the gift tax cost.[3] GRATs can be a very effective way to transfer future growth of rapidly appreciating property, at little or no tax cost. This is achieved by giving a Grantee, whom you name, a remainder interest in your asset. A remainder interest is a future interest in an asset that the Grantor retains the right to own and benefit from, for a predetermined number of years. The crux of this plan is that the gift will be worth less at a later date because a part of the asset has been held back, resulting in a smaller gift and less tax in the future. (Caution: A generation-skipping transfer tax is applied on appreciated assets after the annuity expires. As a result, GRATs are not usually used for transfers to grandchildren, only to children.)

By putting property into a Trust for the benefit of one's heirs but retaining a large enough annuity, or an annuity for enough years, it is possible to substantially reduce or even eliminate all

[3] Florida Statute § 222.14

of the gift tax that would otherwise be due upon the transfer of the asset. For gift tax purposes, the annuity is predetermined at the time of the transfer.

There is a great deal of flexibility in structuring payments under a Grantor-Retained Trust. A Grantor can have the assurance of a fixed annuity under a Grantor-Retained Annuity Trust. Alternatively, a Grantor can protect his or her income against inflation by receiving a fixed percentage of the value of the Trust principal determined annually under a Grantor-Retained Uni-Trust.

Crummey Trust

A Crummey Trust is an Irrevocable Trust. It allows the Trustor to give assets to the Trust which then owns the assets. Therefore, the assets are no longer included in the Trustor's gross estate. This Trust also holds the assets for the beneficiary until some future date. Normally, the IRS will not allow the Trustor to remove assets from the estate unless the beneficiary has a "present interest" in the property. Holding the property for some future use in the Trust does not satisfy the IRS rules. However, there are exceptions.

This Irrevocable Trust provides the beneficiaries with the right to withdraw Trust assets in the year the gift is made, in either the amount of the gift or $14,000 (the amount of the annual gift tax exclusion), whichever is less. The right to withdraw is noncumulative. A Crummey Trust works because a beneficiary has an immediate right to withdraw a portion of the Trust assets. This right constitutes a present interest in the property.[4] Thus, a typical "Crummey Power" will provide the beneficiary with the right to withdraw a certain percentage of the property assigned to the Trust. Normally, a letter is sent to the beneficiary informing him of this withdrawal right. This letter is called a “Crummey” letter. If the beneficiary fails to exercise this

[4] *Estate of Cristofani*, 97 TC 74 (1991)

power to withdraw within the specified time, the property will remain in the Trust for later distribution under the terms of the instrument. Crummey Trusts must create a present interest for beneficiaries and not leave the donor complete control over the assets.[5] Traditionally, the use of such a Trust allows greater flexibility in making discretionary distributions among beneficiaries.[6]

<u>Springing Trust</u>

This Trust is used with buy-sell agreements to provide a more equitable distribution between partners. Virtually every buy-sell agreement has a built-in bias in favor of the surviving owner or owners.

For example, assume two stockholders, Y and Z, each own one-half of the stock in a corporation valued at $1 million. Under the traditional approach to designing buy-sell agreements, (either cross-purchase or stock redemption), the owners would obligate themselves and their heirs to sell the stock interest for $500,000. If Y dies and the stock interest is sold to Z pursuant to a cross purchase agreement, or to the corporation pursuant to a redemption agreement, Y's family gets $500,000 cash and Z gets a business worth $1 million (providing the business value is not depressed by Y's death).

Now assume that Z dies shortly thereafter leaving the business to his family. Under these circumstances, because Y died first, his family gets only $500,000 whereas Z's family gets a million-dollar business.

The use of a Springing Trust provides a technique which can compensate for this built-in bias favoring the surviving owner or owners. It is not necessary to disturb the existing buy-sell agreement which can be left in place together with current life insurance funding.

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[5] *Estate of Outwin*, 76 T.C. 153 (1981)
[6] *Crummey v. Commissioner,* 368 F.2d 82 (9th Cir. 1968)

In order to implement this Springing Trust, Y and Z, as co-Grantors, establish a single Irrevocable Life Insurance Trust (i.e., they both sign the Trust document as Grantor). Funding the Trust with a $500,000 first-to-die policy, insuring both Y and Z, provides a death benefit upon the first death of either one of them. Although individual policies could be used, the first-to-die policy appears to more efficiently provide the funds required at the first death. This Trust is made irrevocable in order to ensure that the proceeds are excluded from the decedent's taxable estate.

The beneficiaries named in the Trust are contingent in that they are the spouse and children of the first to die of either Y or Z. The contingent nature of the beneficiary designation is what gives the Springing Trust its name (i.e., the beneficiaries of the insurance "spring" forward once the policy pays a death benefit). The Trust document is drafted similarly to the typical Irrevocable Life Insurance Trust except for having co-Grantors and the provisions for contingent beneficiaries.

21 Trust

The high gift, estate tax, and generation-skipping transfer tax rates are compelling reasons to use the annual $14,000 gift tax exclusion. If your children are under the age of 21, however, you may not want to use this $14,000 gift tax exclusion (or $28,000 if you and your wife each give to a child,) because a child of tender years may not be able to properly manage the funds. Establishing a 21 Trust allows you to give $14,000 to a child but retain control of the money until the child reaches the age of 21. If a 21 Trust (originating from IRS Code § 2503(C),) is used then certain criteria must be met before you can qualify for the $14,000 annual exclusion.[7]

[7] Internal Revenue Code § 2503(c)

- The Trust must be set up to benefit a minor child.
- The Trustee must have the ability to use the income for the benefit of the minor child without restriction.
- The Trust assets must be invested in income-producing assets (stocks, bonds, and CD's, but not raw land). When the child reaches age 21, the Trust must be distributed to the child. The child can be given the right to require that the assets of the Trust be distributed when he or she reaches age 21, but voluntarily choose not to take the money. Giving the child the right to take the money may increase the risk of the child's obtaining the assets of the Trust at an early age, but it is a safer approach than giving the money outright to a minor child. If the child dies prior to age 21, the Trust assets must be distributed to the child's estate or in a manner that the child appointed.

Special Needs Trusts. A Special Needs Trust is a Trust authorized by federal law which allows a Trustor to include someone within their distribution that relies on governmental needs-based programs (such as Medicaid or SSI benefits) to remain qualified for those programs despite inheritance.[8] The distribution of Trust payments is determined by the Trustee, who has discretion with regard to amounts to be distributed to the individual. Because the beneficiary has no control over income or principal, it is not counted as an asset of the beneficiary. However, the Trustee can only use the assets for the benefit of the named beneficiary and the specified purposes. The Trustor can also determine the successor beneficiary to the Special Needs Trust once the initial special needs beneficiary dies.

PRIT (Personal Residence Trust)

A Personal Residence Trust (PRIT) can be used to remove a large personal asset, namely your home, from your taxable estate with only a moderate gift tax cost. This estate planning strategy involves the transfer of personal-use property, your home, to a Trust similar to those described above. You retain the right to use the asset (living in your home - analogous to the right to an annual income payment made with a GRAT or GRUT) for a set number of years, after

[8] 42 United States Code § 1396p(d)(4)(c).

which the home goes to the persons you designate in the Trust agreement (remainder beneficiaries). [9] PRITs are discussed further in Part X of this Seminar.

Q-DOT (Qualified Domestic Trust)

The federal estate tax is imposed on the taxable estate of every non-U.S. citizen for property located only in the United States. To prevent a non-citizen spouse from inheriting property from a U.S. citizen and then leaving and removing the property from the United States, the unlimited marital deduction is not available to the non-citizen spouse. Therefore, there will be inheritance taxes due upon the death of the U.S. citizen spouse when a non-citizen spouse is the beneficiary. In order to avoid paying inheritance taxes upon the death of the first spouse in this situation, the IRS has allowed for a special Trust to be established, namely the Qualified Domestic Trust (Q-DOT).[10] The Q-DOT is routinely integrated into Living Revocable Trusts or A/B Trusts. If the assets subject to the non-resident alien laws are placed in a Q-DOT, then there will be no taxes due when the U.S. citizen spouse dies prior to the death of a non-U.S. citizen spouse. Q-DOTs are discussed in more detail in Part X of this seminar.

Dynasty Trust

The term "Dynasty" Trust is often used to describe a Trust created for the benefit of multiple generations. The federal transfer tax system is designed to tax property each time it is passed from one generation to the next. However, a generation-skipping transfer tax exemption is available which allows aggregate transfers of $5,340,000 to be exempt from this tax ($10,680,000 for both husband and wife.) Dynasty Trusts, also called Generation Skipping Trusts, are discussed in more detail in Part X of this Seminar.

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[9] Treasury Regulations § 25.2702-5(c)(8)
[10] Internal Revenue Code § 2056A

ILIT Trust

The Irrevocable Life Insurance Trust (ILIT) is one of the most powerful tools of an estate planner. The primary asset held by this Irrevocable Trust is life insurance. The Trust is used to remove life insurance death benefits from the insured's gross estate.[11] This allows the full value of the life insurance death benefit to provide liquidity for the payment of estate taxes and administrative expenses. ILITs are discussed in more detail in Part X of this seminar.

B. Major Laws Governing Trust Creation and Administration

All types of Trusts in Florida, how they are created, and the rules for administration, are governed by the Trust terms, the Florida Trust Code, and supplemental case law. Upon the death of the Trustor(s) (for a Living Revocable Trust) or otherwise per the Trust terms (depending on the type of Trust) the Trustee will review the Trust document and determine how the Trustor of the Trust wanted the Trust assets to be distributed. The Trustee's job to administer the Trust must be performed appropriately or the Trustee could be subject to removal and even civil and criminal liability.

Trust Terms and the Florida Trust Code

Florida enacted a comprehensive codification of Trust law in 2006 in Chapter 736, modeling the Florida Trust Code (or FTC) after the Uniform Trust Code. The FTC governs definitions, how to create a Trust, duties and powers of the Trustee, Trustee liability, beneficiary rights, and most all other aspects of Trusts. Section 736.0105 of the FTC provides the Trust terms will govern a Trust and the FTC provides default rules on subjects to which the Trust is silent. It can be said that the FTC supplements the terms of the Trust, rather than the reverse. In

[11] Internal Revenue Code § 2042

other words, a Trustor is free to follow the FTC, limit some provisions, or expand upon it. The FTC is only applicable where the Trust terms are silent. There are limits to this construction power, however. Section 736.0105(2) provides the Trust terms prevail over the FTC except:

a) The requirements for creating a Trust (testamentary capacity and formalities).[12]
These requirements are the same for a Will: The testator is 18 or older, of sound mind, and signs in the presence of two witnesses.

b) The duty of the Trustee to act in good faith and in accordance with the terms and purposes of the Trust and the interests of the beneficiaries.[13]

c) The requirement that a Trust and its terms be for the benefit of the Trust's beneficiaries, and that the Trust have a purpose that is lawful, not contrary to public policy, and possible to achieve.[14]
It is important to keep this in mind when clients want to create long-term conditions on inheritance, such as requiring a child divorce their spouse before taking their share.

d) The periods of limitation for commencing a judicial proceeding.[15]
The limitation period is 6 months from the date of receiving a Trust Disclosure statement.

e) The power of the court to take such action and exercise such jurisdiction as may be necessary in the interests of justice.[16]
For example, a Trustor cannot strip the court of personal jurisdiction over a Trustee or require suit be brought in a court other than the circuit court.

f) The requirements for the designation of a principal place of administration of the Trust and the requirements for the designation of a jurisdiction the law of which determines the meaning and effect of the terms of a Trust.[17]
A Trustor is free to choose the Trust’s place of administration as long as it has a sufficient nexus to the Trust, such as where the Trustee, beneficiaries, or assets are located.

g) The jurisdiction and venue. [18]
Like the jurisdictional requirements already mentioned, the Trustor cannot choose a venue for Trust litigation unrelated to the Trust or otherwise contrary to venue rules.

h) The restrictions on the designation of representative.[19]

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[12] Florida Statute § 736.0402
[13] Florida Statute § 736.0801
[14] Florida Statute § 736.0404
[15] Florida Statute § 736.0604
[16] Florida Statute § 736.0202 and § 736.0203
[17] Florida Statute § 736.0108(1) and § 736.0107
[18] Florida Statute § 736.0202, § 736.0203, and § 736.0204
[19] Florida Statute § 736.0306.

A Trustor can designate a representative for a beneficiary to receive notice and other information, but cannot designate the Trustee to serve as a beneficiary's representative.

i) The formalities required under § 736.0403(2) for the execution of a Trust.
This section specifically requires a Trust with testamentary aspects, meaning it disposes of property at death, to comply with the requirement of a Will.

j) The power of the court to modify or terminate a Trust[20] except as provided in § 736.04115(3)(b), and under ss. 736.0413, 736.0415, and 736.0416.
These sections set out when a court can modify or terminate a Trust, such as when compliance with Trust terms are inconsistent with the beneficiaries' interests.

k) The ability to modify a Trust[21], except as provided in § 736.0412(4)(b).
For example, the FTC allows the beneficiaries to modify the Trust by unanimous consent after the Trustor's death. The Trustor cannot take away this right of modification in the Trust terms.

l) The effect of a spendthrift provision and the rights of certain creditors and assignees to reach a Trust.[22]
For example, even with a valid spendthrift provision, a beneficiary's interest can still be reached to meet child support obligations.

m) The Trustee's duty to pay expenses and obligations of the Trustor's estate.[23]
A Trustor cannot prohibit the Trustee from paying valid claims in a probate proceeding.

n) The Trustee's duty to file a notice of Trust at the Trustor's death.[24]
Like the requirement to file the original Will with the court, a Trustee must file a Notice of Trust when the Trustor dies, in the county where the Trustor was domiciled.

o) The right of a Trustee under § 736.0701 to decline a Trusteeship and the right of a Trustee to resign a Trusteeship.[25]
The Trust or a court cannot force someone to accept the position of Trustee.

p) The power of the court to require, dispense with, modify, or terminate a bond.[26]
A court can always require a Trustee to post bond if bond is required to protect the beneficiaries, even when a Trust waives the requirement of bond.

q) The power of the court to adjust a Trustee's compensation specified in the terms of the Trust that is unreasonably low or high.[27]

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[20] Florida Statute § 736.0410-736.04115
[21] Florida Statute § 736.0412
[22] Florida Statute § Chapter 736, Part V
[23] Florida Statute § 736.05053
[24] Florida Statute § 736.05055
[25] Florida Statute § 736.0701
[26] Florida Statute § 736.0702
[27] Florida Statute § 736.0708(2)

The Trustee has a right to a reasonable fee, which is comparable to that of a Personal Representative.

r) The duty to notify qualified beneficiaries of the existence of the Trust, of the identity of the Trustee, and of their rights to Trust accountings.[28]
This information is provided in a Trust Disclosure document and is sent to beneficiaries at the Trustor's death.

s) The duty to provide a complete copy of the Trust instrument and to account to qualified beneficiaries.[29]

t) The duty to respond to the request of a qualified beneficiary of an irrevocable Trust for relevant information about the assets and liabilities of the Trust and the particulars relating to Trust administration.[30]

u) The effect of an exculpatory term.[31]
The Trustor cannot limit the Trustee's liability to beneficiaries for certain actions, such as a breach of Trust.

v) The rights of a person other than a Trustee or beneficiary.[32]
While the Trustor can limit certain rights of the Trustee and beneficiary, it cannot limit the rights of others, such as creditors.

w) The effect of a penalty clause for contesting a Trust.[33]

A term in the Trust that effectively penalizes a beneficiary for contesting the Trust is not enforceable.

The FTC sets out the default responsibilities of Trustees. In particular, when the Trustor dies, the Trustee has a responsibility to notify the beneficiaries of certain information, in what's called a "Trust Disclosure Document." This document not only provides statutorily required information to beneficiaries, but upon receipt, starts the limitation period of 6 months upon

[28] Florida Statute § 736.0813(1)(a) and (b)
[29] Florida Statute § 736.0813(1)(c) and (d)
[30] Florida Statute § 736.0813(1)(e)
[31] Florida Statute § 736.1011.
[32] Florida Statute §§ 736.1013-736.1017
[33] Florida Statute § 736.1108.

which a beneficiary can bring an action contesting the validity of the Trust.[34] The FTC also sets out the following duties and requirements for Trustees:

1. Give written notification of the acceptance of the Trust, the full name and address of the Trustee, and that the fiduciary lawyer-client privilege in § 90.5021 applies with respect to the Trustee and any attorney employed by the Trustee to the qualified beneficiaries within 60 days after the Trustee's acceptance (Fla. Stat. § 736.0813(1)(a)).

2. No bond is required for Trust administration unless the Trust instrument requires it, a beneficiary requests it or a court determines it is needed to protect the beneficiaries (Fla. Stat. § 736.0702).

3. Pay expenses and obligations to the Trustor's estate if the personal representative makes a written request that such funds are needed (Fla. Stat. § 736.05053). The Trustee need not obtain property title insurance until the property is placed up for sale (Fla. Stat. § 736.08105).

4. Notify the qualified beneficiaries of the existence of the Trust, the identity of the Trustor, the right to request a copy of the Trust instrument, the right to accountings, and that the fiduciary lawyer-client privilege in § 90.5021 applies with respect to the Trustee and any attorney employed by the Trustee within 60 days after the Trustee acquires knowledge of the creation of an irrevocable Trust or that a formerly revocable Trust has become irrevocable (Fla. Stat. § 736.0813(1)(b)).

5. Once the Trust becomes irrevocable, furnish a Trust accounting to the beneficiaries annually as well as on termination of the Trust or on a change of Trustee. The accounting should be prepared in a reasonably understandable report. The accounting must show all cash and property transactions, fees, gains, losses, and receipt and distribution of assets (Fla. Stat. § 736.08135).

6. Upon reasonable request, provide the beneficiaries with relevant information about the Trust's assets and liabilities and the particulars of the Trust administration (Fla. Stat. § 736.0813(1)(e)).

7. The Trustee has a duty to file a "Notice of Trust" with the clerk of court in the County of Trustor's domicile. The Notice shall contain the name of Trustor, Trustor's date of death, the title of the Trust, the date of the Trust and the name and address of the Trustee (Fla. Stat. § 736.05055).

8. A Florida Trustee has a duty of loyalty and of impartiality. This means the Florida Trustee must administer the Trust solely in the interest of the beneficiaries and administer the Trust impartially, giving due regard to the respective interest of the beneficiaries (Fla. Stat. § 736.0802-3). Generally, this means a Trustee may not participate in any sale or other transaction for his or her own personal account that involves a conflict between his position as Trustee and his fiduciary interest on behalf of the Trust. All actions by the Trustee must be solely for the benefit of the Trust and not in any way place the Trustee personally in a better position. Any such conflicts of interest between the Trustee and the Trust estate are voidable by the affected

[34] Florida Statute § 736.0604

beneficiaries. The beneficiaries must assert their right and will be able to set aside any offending transaction.

9. A Florida Trustee has a duty to administer the Trust estate prudently as a prudent person would, by considering the purposes, terms and distribution requirements and other circumstances of the Trust and by exercising his or her reasonable care, skill and caution (Fla. Stat. § 736.0804).

10. A Florida Trustee has a duty to incur only reasonable expenses, use special skills and control and protect Trust property. Also, the Trustee must keep accurate records, enforce and defend proper claims, and administer the estate pending the outcome of any Trust contest or other legal proceeding (Fla. Stat. § 736.0805, 736.0806, 736.0809, 736.0810, 736.0811 and 736.08165).

12. A Florida Trustee has a duty not to commingle Trust assets with their own assets (Fla. Stat. § 736.0810(2)).

13. The Trustee is personally liable in certain situations if a breach of Trust has occurred. Absent a breach of Trust, a Trustee is not liable to a beneficiary for a loss or depreciation in the value of Trust property or for not having made a profit (Fla. Stat. § 736.1001-3).

14. Distribute the residuary Trust estate to the proper beneficiaries in a timely manner. Upon termination of the Trust, the Trustee may retain a reasonable reserve for the payment of debts, taxes and expenses (Fla. Stat. § 736.0817).

<u>Common Law</u>

The FTC Section 736.0106 provides the FTC is supplemented by the common law of Trusts and by principals of equity. Case law existing prior to enactment of the FTC still applies to the particular issues to which a judicial opinion relates. However, the FTC was only enacted in 2006. Therefore, there are few judicial opinions that arise from litigation particular to Florida's Trust Code.

C. Who are the Main Parties? Their Duties and Responsibilities to a Trust

A Trust has three main parties, all or some of which may be the same person or entity. The Trustor, also known as the Settlor, Grantor, Creator, and Maker, is the party creating the Trust. The Trustor decides who the other parties will be, and the rules by which the other parties will perform their roles or duties. The Trustee is the party who runs the Trust. The Trustor transfers the Trust property to the Trustee. The Trustee holds legal title to Trust property and manages it for the duration of the Trust. The Trustee has the most important duties and responsibilities, which are owed to the third party to a Trust- the beneficiaries. A beneficiary holds equitable title to the Trust property. Beneficiaries ultimately receive all Trust income and principal. Beneficiaries, however, cannot necessarily dictate when or how they take their benefit.

The Trustor and beneficiary have little to no responsibilities or duties to the Trust. The Trustee, however, owes a great deal of responsibility to the beneficiary. Among the duties are:

1. Loyalty: The Trustee must act with loyalty to the beneficiaries. The Trustee cannot enter into transactions which may present a conflict between his fiduciary duty to the beneficiaries and personal interests. For example, selling Trust property to the Trustee's spouse is inherently suspect as a self-dealing transaction. However, such actions can be overcome with court approval or beneficiary approval.
2. Prudently administer the Trust: The duty to act as a prudent person is an objective standard. When administering the Trust, a Trustee must consider the Trust purpose, terms, distribution requirement, and overall circumstances, and exercise reasonable care, skill and caution.
3. Impartiality: A Trustee cannot favor one beneficiary over another outside of the distribution terms. For example, when two beneficiaries who want a particular asset, such as the family beach house, and otherwise cannot come to an agreement, a Trustee may have no other choice than to sell it and distribute the proceeds.
4. Control and protect Trust assets: This includes maintaining proper insurance on real property, making repairs that would otherwise cause more damage if left undone, and even draining a swimming pool at an empty house to protect against accident and arising liability.

5. Inform and account to beneficiaries: Beneficiaries have a right to certain information relating to a Trust, such as the inventory of assets and nature of any liabilities of the Trust. Without this right, a beneficiary could not properly protect his interests. The Trustee also must provide an annual accounting to the beneficiaries to show all the income and expenses of the Trust.
6. Lend his particular skills to the Trust when needed (such as that of Trustee attorney, CPA, or investment broker). [35]

If at any time a beneficiary wants to challenge a Trustee based on the breach of any of these duties, the FTC provides remedies.[36] Remedies range from removal of the Trustee, damages for losses due to the breach, or a court order to perform certain actions. An action for breach of Trust is appropriate in the circuit courts, not the probate court. [37]

D. Revocable vs. Irrevocable

Revocable Trusts are ones that can be changed or terminated by the Trustor, at any time, or as provided otherwise by the particular terms of the Trust. The Living Revocable Trust, for example, is most often used for estate planning purposes and to avoid probate. Living revocable Trusts become irrevocable upon the Trustor's death, since only the Trustor can change these Trusts. An irrevocable Trust, however, is one that the Trustor generally cannot change, and is usually done for asset protection or tax benefit purposes. A Trustor may create a Trust, transferring his property to the Trustee, with detailed terms on how to use the assets, to exclude giving to the Trustor.

[35] Florida Statutes Chapter 736, Part VIII
[36] Florida Statutes Chapter 736Part X
[37] Florida Statute § 736.0203

Several types of irrevocable Trusts are used for tax purposes. One of these is the ILIT – Irrevocable Life Insurance Trust. It is set up so that life insurance proceeds are not part of the taxable estate. A Charitable Remainder Trust is also one with tax benefits. Charitable Remainder Trusts are Trusts in which beneficiaries receive income of the Trust and a charity receives the principal after a certain period of time. While the Trustor cannot change the contribution, he may retain control over how the assets are invested and may change the charity. Charitable Remainder Trusts both reduce the size of the taxable estate and the Trustor avoids capital gains taxes on the donated assets. Part X of this seminar discusses in more detail some of the irrevocable Trusts used for tax benefits.

Irrevocable Trusts are also used to protect assets from creditors. Generally speaking, a person's creditors can reach assets they can reach. By placing assets into an irrevocable Trust, a Trustor is giving up complete control over and access to his own assets. When a Trustor makes this transfer, the assets are no longer ones a creditor can attach. These "creditors" are not necessarily just collectors of debt or judgments, which many people are not haunted with, but includes Medicaid. Medicaid planning Trusts can allow a person to qualify for Medicaid to pay for nursing home costs without depleting a lifetime of savings. Another benefit to irrevocable Trusts is a Trustor, while giving up control of his assets, can still designate his family members as the beneficiaries, thereby keeping the assets in the family.

E. Choosing Trust Situs

A Trustor should create his Trust under the laws of his state of residence. However, many people outside of Florida who have Trusts already migrate to the state of Florida. Any Trust can designate the law under which it will be governed, as long as there is no violation of "strong public policy"[38] and the law has a sufficient nexus to the jurisdiction chosen. In the absence of such designation in the Trust terms, the FTC provides the law of the state of the Trustor's residence at the time of creation controls.[39]

A factor to consider in choosing or modifying the Trust situs is state of taxation. The federal estate tax applies to estates with at least $5,340,000.00 in 2014. [40] Most states do not impose additional estate taxes. Hawaii, Washington, Oregon, Minnesota, Illinois, Tennessee, New York, Maine, Massachusetts, Rhode Island, Connecticut, New Jersey, Delaware, Maryland, and Washington D.C., however, do impose their own tax on estates, which range from Delaware's $675,000.00 exemption up to $5,340,000.00 in Hawaii and Deleware.[41] Inheritance tax on the other hand, is related to the residence of the beneficiary and therefore not relevant to a Trust situs like estate taxes are.

Another factor a Trustor may consider in choosing Trust situs is the governing law. The Uniform Trust Code has been enacted in 28 states. While many Trust clients are not thinking about choice of law issues in this respect, it is something to consider for both the Trustor choosing a Trust company and the Trustor choosing a friend or family member as successor Trustee. A lay Trustee in a state lacking the uniform Trust code or even any sort of Trust code may have little resources to help him know and perform his duties.

F. Trust Funding Basics

A Trust must be funded in order to exist. Without assets, a Trustee cannot perform the directed duties. In order to fund a Trust, assets must be retitled or payable to the legal name of

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[38] "So You Left Your Trust At Home When you Moved to Florida." H. Allen Shore and Jeffrey A. Kern, *The Florida Bar Journal,* May 2009, Vol. 83, No. 5
[39] Florida Statute § 736.0107
[40] http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Estate-Tax
[41] http://taxfoundation.org

the Trust. The Trustee actually holds legal title to the Trust assets, with the Trustee designation distinguishing his holding title to his individual assets. Funding the Living Revocable Trust is the critical element when creating a Living Revocable Trust. If the Trust is not properly funded, the Trust is of little value.

The funding process is not difficult to accomplish or understand. Typically, most people have three "pots" of assets. The first pot holds personal property. This includes tangible items, such as household goods, (things that you have in your home,) furnishings, jewelry, etc. The second pot contains intangible property such as stocks, bonds, bank accounts and things of that nature. The last pot holds your real property wherever located.

The process of retitling your assets from your individual name to your name or someone else's as Trustee is called "funding." The following are examples of what must be done to transfer particular assets into the Living Revocable Trust, thereby funding the Trust. Most of these examples are also applicable to other types of Trusts.

<u>Bank, Savings and Credit Union Accounts</u>

The mere listing of bank accounts on the transfer of assets schedule attached to the Trust is not sufficient to transfer actual ownership of those accounts. For bank, savings and credit union accounts to be transferred into the Trust, each institution where such accounts are located must be contacted and arrangements made for the accounts to be re-registered in the Trustee's name. This usually requires the execution of new signature cards by the Trustee. It is important to note that the new accounts will continue to use the same social security numbers that were on the original accounts. Some banks mistakenly ask you to get a separate tax ID number to open this account. If this is done, it is incorrect. Your social security number should be used on all Living Revocable Trust accounts.

Some financial institutions require a copy of the Trust and they may have additional paperwork for you or your attorney to complete. If the institution says they require you to close the existing account and open a new account to change the title, you have two options: you can follow that procedure or you change the beneficiary on the existing account to the Trust. Remember, the goal is to have all assets owned by or payable to the Trust at your death to avoid the probate process.

Stocks, Bonds and Mutual Funds

If the Trustor has securities in a brokerage account and those securities are registered in street name (the broker holds the securities in his account and the client receives a statement,) the transfer of those assets is relatively simple. The Trustor instructs the account executive to change the title of the account to the Trustee on behalf of the Trust. An example of the proper manner for taking title to Trust property would be "Husband Sample and Wife Sample, Trustees of The Sample Living Trust Dated June 19, 2013". The account executive should be given the correct name of the Trustee and told how the account is to be titled. Often, the Trust instrument will specifically state the name of the Trust agreement, in which case that name should be used in identifying the account.

If the Trustor owns securities that are not in a brokerage account, he or she may wish to open a brokerage account and give the securities to the account executive for registration. If for some reason the Trustor does not wish to have a brokerage account, the securities must be sent to the transfer agent of record, along with supporting documentation such as signed stock powers.

Closely-Held Stock

Stock owned by the Trustor in a closely-held corporation can easily be re-registered to the Trustee's name by tendering the stock to the transfer agent along with the necessary stock powers. If this closely-held corporation is owned solely by the creator of the Trust, than canceling the original stock certificates and re-issuing them in the name of the Trustee on behalf of the Trust is all that is required to transfer those stock shares into the name of the Trust.

Professional Service Corporations

A professional service corporation is a corporation owned by a professional such as a certified public account, lawyer or doctor. A Trustee cannot be the owner of stock in a professional service corporation. Florida Statute 621.09 specifically provides that capital stock in a professional service corporation can be issued only to individuals who are licensed or legally authorized to render professional services. Florida Statute 621.11 further provides that shares in a professional corporation may be sold or transferred only to another individual who is eligible to become a shareholder of such a corporation.

Partnerships

Unless the partnership agreement stipulates otherwise, there is no prohibition against a Trustee also being a partner in a partnership agreement, either limited or general. Moreover, a partner may assign his or her partnership interest and, unless otherwise provided for by another partnership agreement, the assignment does not dissolve the partnership.

Life Insurance, Annuities and Qualified Plans

The general rule is that a Living Revocable Trust does not become the owner of life insurance, annuities or qualified plans (401K, IRA, etc.). Normally these instruments designate beneficiaries upon the Trustor's death. If a husband dies owning life insurance, his wife is generally the beneficiary of the policy. Beneficiaries have also been selected for annuities and qualified plans. Therefore, these assets will always pass outside probate anyway. One of the few times when life insurance would be retitled in the name of the Trust is when the life insurance policy has a large cash value. Take for example an estate where the husband and wife are cash poor. The husband, as owner of the life insurance policy, may not die but, rather, become incompetent. The wife will have no way of getting to the cash value of the policy to help pay expenses. If that policy is held as an asset of the Trust, then the spouse, as backup Trustee, can step in and use the cash proceeds as needed. In such a case, the Trust will be the first named beneficiary of a life insurance policy. Upon the death of the insured, the proceeds of the life insurance policy will be immediately payable to the Trustee for distribution according to the terms of the Trust. In the case of a married couple, when the husband dies the insurance proceeds will be payable to the wife as the successor Trustee to the Trust. This prevents a situation where the husband and wife both die within a relatively short period of time and the second-to-die spouse receives the insurance proceeds outside the Trust estate. If this occurs, the insurance proceeds must go through probate before passing to the heirs.

Likewise, tax-deductible annuities and qualified plans normally would not be titled in the name of the Trust. These investments have designated beneficiaries and therefore, avoid probate. If these instruments are tax-deferred instruments, the spouse will continue to be listed as the first beneficiary but the second beneficiary should be changed to the Trustee on behalf of the Trust.

Real Property and Homestead

One of the greatest advantages to creating a Living Revocable Trust is the ability to transfer real estate without it going through probate. This specifically includes the transfer of real estate in Florida, as well as every other state where real property is owned by the decedent.

There are many problems associated with the transfer of real estate into a Trust if it is done by an out-of-state lawyer or by using a "do-it-yourself" form from a generic, "one-size-fits-all" book on Trusts. For instance, in Florida, the home where you live takes on a different legal status than does other real property you own. In Florida, one's house is his homestead and it provides certain tax advantages and creditor protection rights. If the appropriate language is included, transferring your homestead property into your Living Revocable Trust will not affect your homestead exemption nor will it affect your protection from creditors. Similarly, transferring the property into a Living Revocable Trust will not waive or destroy the $250,000 exemption from capital gains taxes that can be obtained every two (2) years for all homeowners who sell their property. In essence, all the benefits received now, by ownership of property, will be maintained even though it is owned by a Living Revocable Trust.

Care should be given to the language of the deed that transfers the property into the Trust, as well as the type of instrument used. Many law firms or out-of-state companies use Quit Claim deeds to transfer real property into your Living Revocable Trust. The problem with using a Quit Claim Deed is that such a deed does not make any warranties of title. This could result in the owner losing any title insurance protection that he previously had. It is preferable to use a Warranty Deed to convey title that normally provides the grantee with prior title warranties.

With only two exceptions, including Alabama, every other state within the United States allows the transfer of property from an individual to an individual's Trust without the payment of documentary transfer stamps. Documentary stamps are the states' tax upon the real estate conveyance. Florida assesses documentary stamps at the rate of $7 per $1,000. That means if your property is worth $1,000, you will owe $7 in documentary stamps. These stamps are not assessed on property transferred to a Living Revocable Trust (except for the $.70 minimum when recording the deed to the Trust). The only fees assessed in Florida are the recording fees and an indexing fee. The recording fees are normally $10 for the first page, $8.50 for additional pages, plus a $.70 minimum in documentary stamps, and a $1 indexing fee for each name on a deed after the first name. If a husband and wife transfer property from themselves, individually, to themselves as Trustees, then the total cost of recording is typically $19.20. In most other states the recording fees vary from $15 to $30 per deed. A few states require small transfer fees that amount to no more than $30 or $40.

Some states, such as Pennsylvania, require the recording of the Trust instrument. It is wise to include with a Trust, a summary of the Trust for recording purposes. This allows the Trust to be recorded but keeps the personal information private. There are only a few states that require the recording of the Trust instrument. Most states simply require the recording of the deed and other miscellaneous transfer forms and related documents. Generally, funding a Trust with real estate in the state of Florida takes two to four weeks.

Funding a Trust with real property owned in any other state may take longer depending on that state's requirements and the transfer forms involved. There are forty-nine other states and each state has numerous counties (Florida alone has 67 different counties.) These counties operate like little empires and the recording requirements and necessary forms can vary from county to county within each state. It is best to have either a great deal of patience or to contact a local attorney in the county where the land is located to record the deed to your Trust.