Estate Planning with Revocable Trusts

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For many people, creating an estate plan is dreaded, and a "check-the-box" item never to think about again. Yet, estate planning should be a foundational aspect of a person's financial life and wellness. The traditional approach to delineating one's final wishes and dispositive plan is to build and execute a Last Will and Testament. And while everyone needs a will, there is an alternative approach known as the revocable trust that includes one's dispositive wishes. Dispositive wishes are how your "stuff" flows after you die – to heirs, to charity, or elsewhere, whether in trust, or outright.

A revocable trust is a vehicle by which a grantor, or creator of the trust, titles assets to the trust and appoints a trustee (which may be themselves) to oversee the management and administration of the assets of the grantor while they are living, and the trustee (or successor trustee, if the grantor originally served) continues the trust administration after the grantor passes, providing that the grantor's dispositive wishes were included in the trust language. Often revocable trusts are coupled with a simple, "pour-over" will, which states any assets that were not previously titled into the trust and instead pass via the will are to be added to the revocable trust upon death (or poured over into the trust). Revocable trusts - also called "living trusts" or "inter-vivos trusts" – are set up while the grantor is living and may hold different types of assets, including marketable securities, real and personal property, and other assets. Revocable trusts can also be joint trusts, serving as one trust for the benefit of a married couple, with the same benefits and features applying to both spouses as grantors. Below, we discuss some of the details of revocable trusts.

Assets titled to a revocable trust are not subject to the probate process.
A funded revocable trust (one that has assets titled to it) will speed up the dispositive process and simplify estate administration, while providing a measure of privacy to the decedent. The administration process for the trust assets would not be delayed by potential court scheduling or waiting for third parties to act, as would be the case with assets passing via a traditional Last Will and Testament. The trustee of the trust can act with authority on matters pertaining to the assets titled to the trust.

A revocable trust provides for continuity via a successor trustee in the event of incapacity. A revocable trust is a helpful incapacity planning tool because in the event of a temporary or permanent loss of cognitive abilities, the named successor trustee can assume the reins and make sure everything continues to run smoothly, including bills being paid, gifting completed, healthcare provided, and assets protected.

Out of state property owned in a revocable trust avoids ancillary probate. If someone owns real estate in a state other than their state of residence, an additional probate proceeding must take place in the state the property is located, called an ancillary probate proceeding. The probate court in the decedent's home state has no legal jurisdiction over out-of-state property, so ancillary probate is necessary. On the contrary, if the real estate is titled to a revocable trust, there is no need for the ancillary probate because the assets are distributed by the Trustee after death, potentially saving additional legal fees and time.

A joint revocable trust with TN Community Property Provisions:

- A unique feature available to joint revocable trusts in the state of Tennessee is the Community Property provision. This allows for equal ownership of property by husband and wife, including a sharing in appreciation and income from the property. Tennessee is not a community property state; however, you can elect for a trust to have community property treatment based on a Tennessee trust law first passed in 2007.
- A "Community Property Trust" can provide significant income tax advantages, such as a full step up in basis of trust assets at the first spousal death, and a possible second full or partial step up in tax basis at the second spousal death. What that means is the cost value of the entire sum of the assets held in the community property trust is given a new cost value equal to the market value of the property as of the date of death of the first spouse. This of course drastically reduces capital gains taxes in the event the trust property is sold after the death of the first spouse.
- For example, say you paid $500,000 for a portfolio of stocks and held them until your death, when the value had appreciated to $1,000,000. If the portfolio had been held JTWROS (Joint Tenants with Rights of Survivorship) with your spouse, upon your death, your half of the property would receive a step-up in basis to $500,000 (half of the fair market value of $1,000,000), but the spousal half would remain the same ($250,000, or half of the original purchase price of $500,000). Your spouses' basis is now $750,000 and if he/she were to sell the stock following your death, he/she would realize a gain of $250,000, and pay long term capital gains tax on that amount, which could be up to $59,500 at the current maximum 23.8% rate.
- However, if the assets were held in a trust with community property provisions, the entire value of the assets would receive a step-up in basis to $1,000,000 at the death of the first spouse. If the survivor then sold the assets, they would have a capital gain of $0 and pay nothing in capital gains tax due to the stepped-up basis of the entire amount, as opposed to only the half owned by the deceased spouse. Moreover, if the assets

involved include rental real estate or certain other assets, there could be re-depreciation following the step up. This feature provides the surviving spouse with greater flexibility and the ability to sell a home to downsize, re-construct an investment portfolio to provide more income, or extract liquidity from previously capital-gains-tax-encumbered assets.

- The requirements for a trust to be treated with community property laws are as follows: the trust agreement must state that it is a community property trust; the trust must have at least one trustee who is a Tennessee resident or a Tennessee bank or trust company; the trust must be signed by both spouses; and the trust must contain a statutory warning that gives notice of the potential consequences of this provision during marriage and in the event of a divorce.
- A revocable trust with community property provisions should be carefully considered by happily married couples who have large amounts of unrealized gains, whether in marketable securities, real estate, or other assets.

When was the last time you looked at your estate plan? Have you considered the different approaches to passing your assets and values? Perhaps your current plan was once appropriate, but laws have changed, or maybe your assets or family have changed. The Truxton team can help you think through these considerations as a critical component of our role in managing your wealth. If you would like to discuss your situation or have your questions answered, please give us a call. We are happy to help! ▪