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Choosing the Ideal Trust for Your Wishes

The term *estate* may bring to mind mansions, vast fortunes, and a level of wealth that many people do not possess. This misconception may lead to the false impression that estate planning is only for the rich and famous, discouraging those with more modest means from seeking professional guidance.

If *estate* is a loaded term, then *trust* is even more so. Mention the word *trust*, and many people think of wealthy families, complex legal arrangements, and a level of sophistication that can seem intimidating or unnecessary.

Misconceptions about trusts often stem from a lack of understanding about what a trust actually is, how it works, and situations where it can provide benefits above and beyond a will. Wills and trusts are complementary—not mutually exclusive. They can serve different roles in an estate plan and often address different concerns.

Trust Basics

Trusts can work in various ways depending on the type of trust and how you want to pass down your *assets* (accounts and property). However, every trust has some things in common.

When you transfer assets to a trust, the trust becomes the legal owner of those assets. You are, in effect, giving up direct ownership of whatever assets you place in a trust, which can include real estate, bank and financial accounts, personal property, and even things such as life insurance proceeds and business interests.

- As the *trustmaker* (sometimes called the trustor, settlor, or grantor), you create the trust and decide which asset(s) to put into it.
- A *trustee* (or co-trustees) manages the trust on your beneficiaries' behalf. Depending on the type of trust you create, you might be the initial trustee.
- Your *beneficiaries* receive proceeds from the trust based on instructions you leave the trustee in the trust agreement. You can give the trustee wide discretion to manage assets or prescribe very narrow parameters. Depending on the type of trust, you might also be the beneficiary while you are alive.

Although a will can also be used to name beneficiaries to receive your assets, it takes effect only after you die. A trust, on the other hand, is effective during your lifetime, which means that a *successor* (backup) trustee can step in to manage your assets if you become disabled or injured—not just when you pass away, as with a will.

People create trusts for numerous reasons. Some of the most common are the following:

- **Avoiding probate.** The court process known as probate imposes additional costs, delays distributions, and is part of the public record. Assets held in a trust avoid probate. They pass directly—and, in most situations, privately—to beneficiaries according to the instructions you have included in the trust agreement.
- **Reducing estate taxes.** If your net worth exceeds exemption amounts for estate and inheritance taxes, certain types of trusts can help minimize your tax liability, leaving more money to benefit your loved ones.
- **Protecting assets.** Trusts can shield assets from the beneficiary's creditors, lawsuits, and potential financial mismanagement.

- **Providing for loved ones.** Trusts can ensure that loved ones, such as minor children or those with special needs, are cared for according to your wishes.
- **Managing assets during incapacity.** A trust allows for the seamless management of assets if you become *incapacitated* (unable to manage your affairs), ensuring estate plan continuity and avoiding potential court intervention.
- **Charitable giving.** Trusts can be used to support charitable causes and provide associated tax benefits.
- **Incentivizing behavior.** You could structure a trust to encourage beneficiaries to achieve certain goals, such as pursuing education or maintaining employment.

Demand for trusts is increasing as Americans go through the "Great Wealth Transfer" from older generations to younger family members.[1] Ultimately, the decision to create a trust reflects a desire for greater control, protection, and flexibility in managing and passing down wealth.

Trust-Based Planning Scenarios

Understanding how trusts work can help you properly visualize how a trust might fit into your own estate plan. To further illustrate the variety of roles trusts can play in achieving your legacy goals, here are some specific examples of scenarios where trusts are commonly utilized:

- **You have a high net worth** (specifically, a net worth exceeding the federal estate tax exemption, or state exemption levels, which are as low as $1 million in Oregon and even lower in some states that impose an inheritance tax). If these taxes affect you, consider
  - **a grantor retained annuity trust**—allows you to transfer assets to beneficiaries while retaining an income stream;
  - **a charitable remainder trust—**provides an income stream to beneficiaries, with the remainder going to a designated charity; or
  - **a dynasty trust**—passes wealth down through multiple generations.
- **You want complex distribution instructions**, which could involve blended families, beneficiaries with special needs, or beneficiaries who are prone to financial mismanagement or vulnerable to creditors. These scenarios may lend themselves to
  - **a spendthrift trust—**protects assets from creditors and prevents beneficiaries from squandering their inheritance;
  - **a supplemental needs trust—**enables a disabled beneficiary to receive financial support from the trust without affecting their eligibility for means-tested government benefits;
  - **an incentive trust**—makes distributions to a beneficiary dependent on their meeting certain conditions, such as graduating, becoming employed, getting sober, or volunteering for charitable causes; or
  - **a qualified terminable interest property trust**—provides for a surviving spouse while ensuring that the deceased spouse's assets ultimately pass to their chosen beneficiaries when the surviving spouse dies.
- **You are exposed to unique tax liabilities** related to situations such as having extensive real estate investments or business ownership. Possible trust solutions include the following:

[1] Ronda Lee, *More Americans are dealing with tax filings for trusts as older boomers pass away*, Yahoo! finance (Apr. 5, 2023), https://finance.yahoo.com/news/more-americans-are-dealing-with-tax-filings-for-trusts-as-older-boomers-pass-away-211151632.html.

- **a qualified personal residence trust**—allows for the transfer of a primary residence or, in some circumstances, a vacation home, to a trust while retaining the right to live in it for a set period or
- **an irrevocable life insurance trust**—holds a life insurance policy that uses the death benefit proceeds to cover estate taxes or provide liquidity to a business after your death.

Estate planning attorneys often emphasize that every adult, no matter their age or wealth level, needs an estate plan. It should start with a will, but depending on your financial and family situation, a trust can be a valuable addition to your plan.

If you think a trust may be right for you and your family but are overwhelmed by the number of options and their range of uses, set up a time to talk with us about the different trust types and the benefits they offer.