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## Living Trusts

### What is a trust?

A **trust** is a relationship in which a person (or business) holds title to property for the benefit of another person. The terms of this relationship are usually described in a written document, which is commonly called a **trust instrument, trust agreement, declaration of trust** or simply **trust**.

### Who are the parties to a trust?

The creator of the trust is commonly called the **settlor, trustor, or grantor**. The person (or business) holding title to the property for the benefit of another is called the **trustee**. A person for whose benefit the trust was created is called a **beneficiary**. The grantor may choose to be both a trustee and a beneficiary of the trust. However, a valid trust is not created if one person is both the sole trustee and the sole beneficiary.

### What is a "living trust"?

A **living trust**, also known as an **inter vivos trust** (inter vivos is Latin for "between the living"), is a trust created during the lifetime of the grantor. It is to be distinguished from a **testamentary trust**, which is a trust created through a will. Sometimes people confuse a living trust with a living will. A **living will** is a document a person signs stating their wishes about being kept alive by artificial means, and has no similarity to a living trust and is not an estate planning device.

## **What is a "revocable grantor trust"?**

The term "living trust" is often used to refer to a specific type of living trust – a **revocable grantor trust**. The grantor is the trustee of the trust and is also the sole lifetime beneficiary. A successor trustee is named to serve if the grantor becomes disabled or dies. Successor beneficiaries are named to receive assets at the grantor's death. The grantor may revoke the trust or modify its terms at any time until he or she dies or becomes legally incapacitated. This right to revocation gives the grantor flexibility with his or her assets making this type of trust the one people most often choose.

## **How does a revocable grantor trust avoid probate?**

Probate administration is the court process to distribute property owned by an individual at death. It is distributed in accordance with the individual's will, or according to state law if there is no valid will. If an individual owns no property at death, there is normally no need for probate administration. By creating a revocable grantor trust and transferring all of your property to the trust, you can avoid owning any property in your name alone at death, and consequently avoid the need for probate administration. The terms of the trust can provide directions to the successor trustee on how to distribute the trust property after the grantor's death. In this way, the trust acts much like a will, except that no probate court involvement is necessary.

## **Will a living trust save me money?**

A living trust will never save money for the person who creates it, for the reason that there is a cost for the preparation of the trust document and the associated documents required to fund the trust. In addition, if realty is sold from the trust, before or after the death of the grantor, a certificate of authority that the trust allows the trustee to sell the property, is probably going to be required. There will be extra costs for this as well as any possible amendments to the trust. The successor trustee will most likely need legal counsel in complying with the requirements of the trust and paying any applicable death taxes. If there is no probate estate, then recent changes to Michigan law require that the successor trustee publish a notice to allow creditors to file a claim against the trust. If there are no assets with which to pay a claim, e.g., because the assets have already

been distributed to beneficiaries, **then the trustee becomes personally liable**. Since it is advisable to have an attorney draft the necessary documents, additional costs will be incurred. Many trusts have lay persons, e.g. relatives, named as successor trustees, who serve with nominal or no compensation. If a corporate trustee is named, such as a bank, the fees can be very expensive. It is possible that the cost of a living trust will be less than the cost of probate. If so, then the living trust you purchase, while not saving you any money, will save money for your beneficiaries.

### **Is my trust responsible for my debts?**

A trust does not protect your assets from claims of creditors. While you are living the assets in your trust can be reached to satisfy court judgments against you. After your death creditors can file a claim against the trust if there are insufficient funds in your probate estate. If the trust is for a married couple it can be reached to satisfy court judgments against either spouse. Real estate and some other assets titled in a husband and wife's name (referred to as **tenants by the entirety**), which is not in a trust, can not be reached to satisfy the individual debts of one spouse. For this reason some attorneys advise married couples to leave their home titled as **tenants by the entirety** and not transfer it into a trust to keep it protected against creditors of one spouse.

### **Can a revocable grantor trust allow one to avoid death taxes?**

No. Avoiding probate does not mean death taxes are avoided. A deceased person's property (even if held in trust) is generally subject to the Michigan Inheritance Tax and federal estate tax if it exceeds \$ 2 million (in 2006-2008; this amount will rise in 2009). Death taxes have complicated rules and many exceptions. Certain trusts can be used to reduce the amount of death taxes due. You should contact an estate planning attorney for specific advice.

### **Can a revocable grantor trust help shelter my assets for Medicaid eligibility purposes if I need long term care as a nursing home resident?**

Under Medicaid rules, the assets of a revocable grantor trust are considered to be available to the grantor because the grantor can terminate

the trust at any time to gain access to trust property. Because the trust assets are considered available to the grantor, they are treated as the grantor's property in determining the value of the grantor's countable assets for Medicaid nursing home benefit eligibility. While a home in Michigan is generally exempt for Medicaid eligibility, it is countable, (i.e. not exempt,) if titled in a revocable trust. In some cases, married couples can benefit by having the home counted as an asset and then transferred out of the trust later.

It also may be possible to shelter assets for Medicaid nursing home eligibility purposes through transfers to an **irrevocable trust** which prohibits the nursing home patient's right to trust benefits. Medicaid penalizes most transfers to trusts made within 5 years of a Medicaid application. Medicaid law is complicated and a number of factors must be considered before such a transfer. **You should contact an attorney if you want to use a trust for Medicaid planning.**

### **What is an irrevocable trust?**

If the terms of a trust do not provide a person with the power to amend or revoke the trust, then the trust is an irrevocable trust. In most circumstances, this means that the trust assets cannot be retrieved from the trust nor used in a manner inconsistent with the terms of the trust. Thus, careful consideration should precede the transfer of assets to an irrevocable trust.

### **Can I create a trust on my own?**

Although it is not illegal to draft your own trust, the complexities of property and tax law make it risky. The advice and counsel of an experienced attorney is strongly recommended. It is also advisable to have an attorney draft the documents necessary to fund the trust. "Trust kits" advertised for sale in many publications may provide a number of generic fill-in-the-blank forms. However, the forms provided are not necessarily tailored to your specific situation. Sometimes there are insufficient instructions for "funding" the trust, an essential aspect of having a trust to avoid probate. Funding the trust means transferring assets owned by the grantor into the name of the trustee. If this isn't done, the assets will have to go through probate at the death of the grantor. Whether the transfer of assets is done by the grantor or an attorney, it is a very

important part of the trust and a failure to fund the trust is probably the biggest reason some trusts fail. It is also important to be aware that Michigan law treats a trust as a separate legal entity from the grantor. Because of this it is imperative that insurance coverage of any asset transferred to the trust must be modified to reflect the change. In addition, planning factors peculiar to the laws of your state may not be considered in the forms provided. Finally, the instructions provided for completing these "trust kits" commonly recommend that you take the completed forms to a local attorney for review before executing them. An attorney presented with such forms may reject them in favor of his or her own trust forms, leaving you with the same attorney's fee you would have paid without the "trust kit".

More often what is encountered is a trust marketed and offered by some type of organization, sometimes owned by an attorney, but frequently not. Seminars for "free estate planning advice" and direct mail solicitations are targeted at seniors. Things to be wary of are misrepresented facts about commonly used probate avoidance techniques and the need for and cost of a living trust, and exorbitant costs running two to three times as much as an estate planning attorney might charge. Before you sign on the dotted line, it would be a good idea to check with the Legal Hotline for Michigan Seniors, the State Bar of Michigan, or the Consumer Protection Division of the Michigan Attorney General's office.

### **Is a revocable grantor trust expensive to create?**

For a given estate plan, the fee charged by an attorney for the preparation for a revocable grantor trust will usually exceed the fee for the preparation of a will. Because attorneys generally set their fees based upon time, the higher fee for a revocable grantor trust may be explained, at least in part, by the extra time involved setting up a revocable grantor trust as part of your estate plan. This work includes drafting the trust and any accompanying instruments, such as a pour over will (see next question), assisting in the execution of all instruments, and funding the trust, that is, transferring property to the trust.

### **If I have a revocable grantor trust, do I still need a will?**

Yes. An estate plan employing a revocable grantor trust is normally accompanied by a **pour-over will**. A pour-over will transfers any property

solely owned by the grantor/testator at death to the trust. In this way, it "pours" the probate estate over into the trust. Although the grantor may have transferred all of his or her property to the trust to avoid probate, a pour-over trust is needed to act as a safety net, catching any property that was not transferred to the trust before death.

## **Should I have a living trust?**

The use of a living trust to avoid probate is not new – trusts have been around for a long time. They have typically been used in large estates, not only for the possible avoidance of death taxes but also to avoid the costs of probate, which are higher for larger estates because there is often more complexity, work and fees. What is new is the marketing of living trusts to people with small or modest – sized estates. In many of these situations a living trust may or may not make sense, may or may not save money. Because a living trust has a cost, it is never a "savings" to the person making it, but intended to save money for the person's heirs. It is possible that in some situations it might be a better decision to invest the amount of money a trust would cost; the investment could grow to be worth more than the cost of probate. As mentioned earlier, one can incur additional, extra costs, beyond the initial one for preparation of the documents. And, there are other, low cost options for avoiding probate. If you are considering a trust you should consult with a lawyer knowledgeable in estate planning and carefully review all of your options, given your particular situation.

If you have additional questions concerning living trusts or other legal matters, and are a Michigan resident and 60 years of age or older, you can call the Legal Hotline for Michigan Seniors at **1-800-347-5297** or **(372-5959 for the Lansing area)** weekdays between 9 AM – 5 PM.

*The Legal Hotline is a program of Elder Law of Michigan, INC., a non-profit organization. If you would like to support our work, please consider sending a tax deductible donation to the Legal Hotline, 3815 W. St. Joseph, Suite C-200, Lansing, MI 48917. Thank you.*