Living Trust and Estate Planning Basics

WHAT YOU NEED TO KNOW

THE WERNER LAW FIRM

Introduction

There is one question you need to ask yourself. It is the one, fundamental question that this book addresses, and that the estate planning profession as a whole deals with:
If something bad were to happen to you today, what would happen tomorrow?

The reality is, we are human. We procrastinate. We think we are immortal, and we generally think everything will work itself out. It is natural to feel this way, but this combination of traits can be particularly devastating when applied to estate planning.

As an attorney, I can assure you that these things do not magically work out. Think about your family, your home, your financial assets. If something happened, would someone be able to step in to take care of things? Who would be in charge? Who would inherit what? How would minor children be taken care of? Would there be fighting between family members? Does your family know about the different bank accounts, life insurance policies, retirements accounts that you have?

If you were disabled and unable to make decisions for yourself, would somebody be able to deal with your doctors, pay your mortgage, etc.? Who would that be? These are issues that everybody needs to address, not just people who have families or are wealthy.

Back in the days of the wild west, it might have been relatively easy to walk down to the local courthouse and have the neighborhood judge address these issues. One hundred and seventy years of California legislation changes things dramatically. Yes, if you do nothing, things will eventually be sorted out. But there is a reason that people know that probate court is bad and should be avoided. It can take well over a year, cost tens of thousands of dollars, and ultimately, it likely will not go the way you would have intended.
This is why I am writing this. It doesn't have to be this way. I want to educate you and our community on how to address these issues. I do not want families to have to deal with the burdens of probate court, particularly at a time of loss when they should be focused on more important matters.

Setting up your plan is probably much easier than you would think. And once set up, these are documents that could potentially last the rest of your life. So spend the time. By next month, you could have everything squared away in a nice binder, full of instructions for you and family members, and not have to worry about any of this anymore.
All you have to do is start.

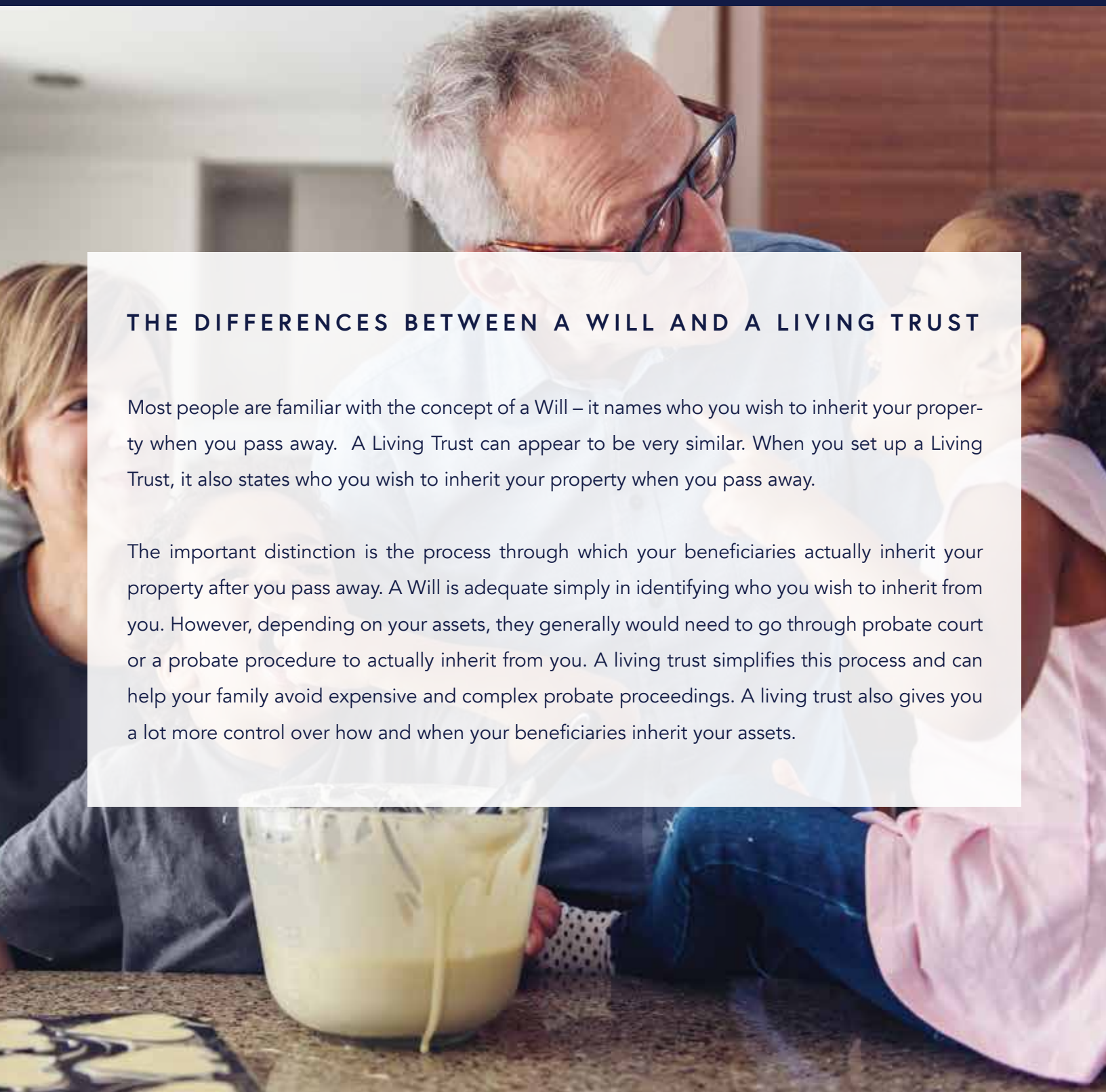
The Werner Law Firm

Troy Werner, Esq.

THE BASICS

The goal of establishing a living trust, will, or other legal documents is to allow for the proper transfer of your property after death.

This process – called estate planning – determines who will receive your property and how it will be distributed after you pass away, as well as setting guidelines on who you trust to carry out those wishes.



THE DIFFERENCES BETWEEN A WILL AND A LIVING TRUST

Most people are familiar with the concept of a Will – it names who you wish to inherit your property when you pass away. A Living Trust can appear to be very similar. When you set up a Living Trust, it also states who you wish to inherit your property when you pass away.

The important distinction is the process through which your beneficiaries actually inherit your property after you pass away. A Will is adequate simply in identifying who you wish to inherit from you. However, depending on your assets, they generally would need to go through probate court or a probate procedure to actually inherit from you. A living trust simplifies this process and can help your family avoid expensive and complex probate proceedings. A living trust also gives you a lot more control over how and when your beneficiaries inherit your assets.

WHAT'S BETTER FOR YOU? A LIVING TRUST OR A WILL?

Living trusts are generally preferred when you own real property, if you have a large estate, or if you have minor children. Almost everyone who owns real property in California should have a living trust. If you simply had a will, your home and other real property would still need to be transferred out of your name on death. Naming a beneficiary in a will would simply advise the court who you want to inherit the property, but they would still have to go through probate or a probate procedure in order to effect that transfer of ownership. A living trust avoids this issue entirely.

Additionally, with a living trust, you also have a lot more freedom to control your property after you pass away. For example, if you have minor children, you can set up the trust so that they receive property or other assets such as life insurance when they reach a certain age, or even have multiple distributions when they reach certain ages. For instance, instead of receiving assets outright at age 18, a trust can state that they would receive 1/3 of their share at age 22, 1/3 at age 25, and 1/3 at age 30.

Also, if you have other family members or beneficiaries who you wish to provide for, but who you do not want to have receive a large sum of money immediately, your trust can instead set aside money for the benefit of those individuals. For example, if you have a family member who has special needs or is otherwise unable to take care of themselves, or you simply have a beneficiary who is financially irresponsible, the trust can be set up such that you set aside a specific sum of money for their benefit which would then be managed by the person you put in charge of the trust after you pass away: your successor trustee. That person would then manage the funds for your beneficiary and would be able to do things such as paying for your beneficiary's rent, living expenses, utilities, tuition, bills, or other various expenses, all to the benefit of your beneficiary.

If you're not sure, we can discuss your goals and help you determine the best option for you.

HOW A LIVING TRUST WORKS TO AVOID PROBATE

When you create a revocable living trust, you transfer any property you want the trust to control into the trust. This generally will include any homes, real property, and financial accounts. For example, if you own a home, the title of your home would then be held by your trust, instead of under your name as an individual.

While you are alive, you control and manage the living trust. This means that you have the ability to change the trust to suit your wishes at any time, and you retain control over the assets controlled by the trust. You do not have to do anything new or special when filing taxes or with regards to the mortgage. These assets are still treated as your assets. You can sell your property, move, and generally exercise the same control over your property that you could before you set up the trust.

Then, once you pass away, the person you put in charge of the trust (your successor trustee) can step in and immediately start dealing with trust assets without having to go through probate court! This is because the assets are titled in the name of the trust, and they are stepping in to act as the trustee in your place. You generally will also name backups in the trust, so if the person you designate as your successor trustee is unable to handle it, your backup will be able to step in to take care of things.

PROVIDING FOR PETS IN YOUR LIVING TRUST OR WILL

Many attorneys do not take the time to address this, but if you have a specific person you wish to designate to take care of your pets, we are happy to include this instruction in your trust or will. Additionally, you can even set aside a specific sum of money for the benefit of your pet.

HIRING A LAWYER VERSUS DO IT YOURSELF OPTIONS

We sometimes compare hiring an estate planning attorney to hiring a mechanic.

If something is wrong with your car, as an intelligent person, you could probably spend the time and effort to educate yourself on what is wrong and attempt to fix it. With trial, error, and some potential mistakes, you could probably repair it yourself. That being said, there is a reason most people hire a mechanic. It is easier and they want it done properly the first time by a professional.

Creating a living trust and estate plan is a complicated matter. We have spent years as attorneys dealing with various situations, and trust language is constantly evolving. It is easy to make mistakes in "do it yourself" trusts, and such mistakes can be devastating. Unlike repairing a vehicle, where you could test drive it, a mistake in a trust generally will not be discovered until after you pass and it is already too late.

We commonly deal with the aftermath of flawed trusts, and such mistakes can usually result in your beneficiaries having to go through probate. At worst, we have seen improperly prepared trusts confuse important terms, leave assets to the wrong beneficiaries, and cause beneficiaries to even engage in lawsuits against one another. Ambiguous or unclear language in these documents can be devastating. These mistakes can end up costing beneficiaries substantially more in terms of time and money than what would have been spent on a professionally done trust. As discussed in our probate section, probate fees are based on the gross value of the estate and can easily cost tens of thousands of dollars.

Here are some third-party articles that discuss using a lawyer versus online legal services and Do-it-Yourself options for Estate Planning:

Should you Hire an Estate Planning Attorney or DIY?
https://momanddadmoney.com/should-you-hire-an-estate-planning-attorney-or-diy/

Don't Buy Legal Documents Online Without Reading This Story
https://www.marketwatch.com/story/dont-buy-legal-documents-online-without-reading-this-story-2015-11-23

Legal DIY Websites Are No Match For A Pro
https://www.consumerreports.org/cro/magazine/2012/09/legal-diy-websites-are-no-match-for-a-pro/index.htm

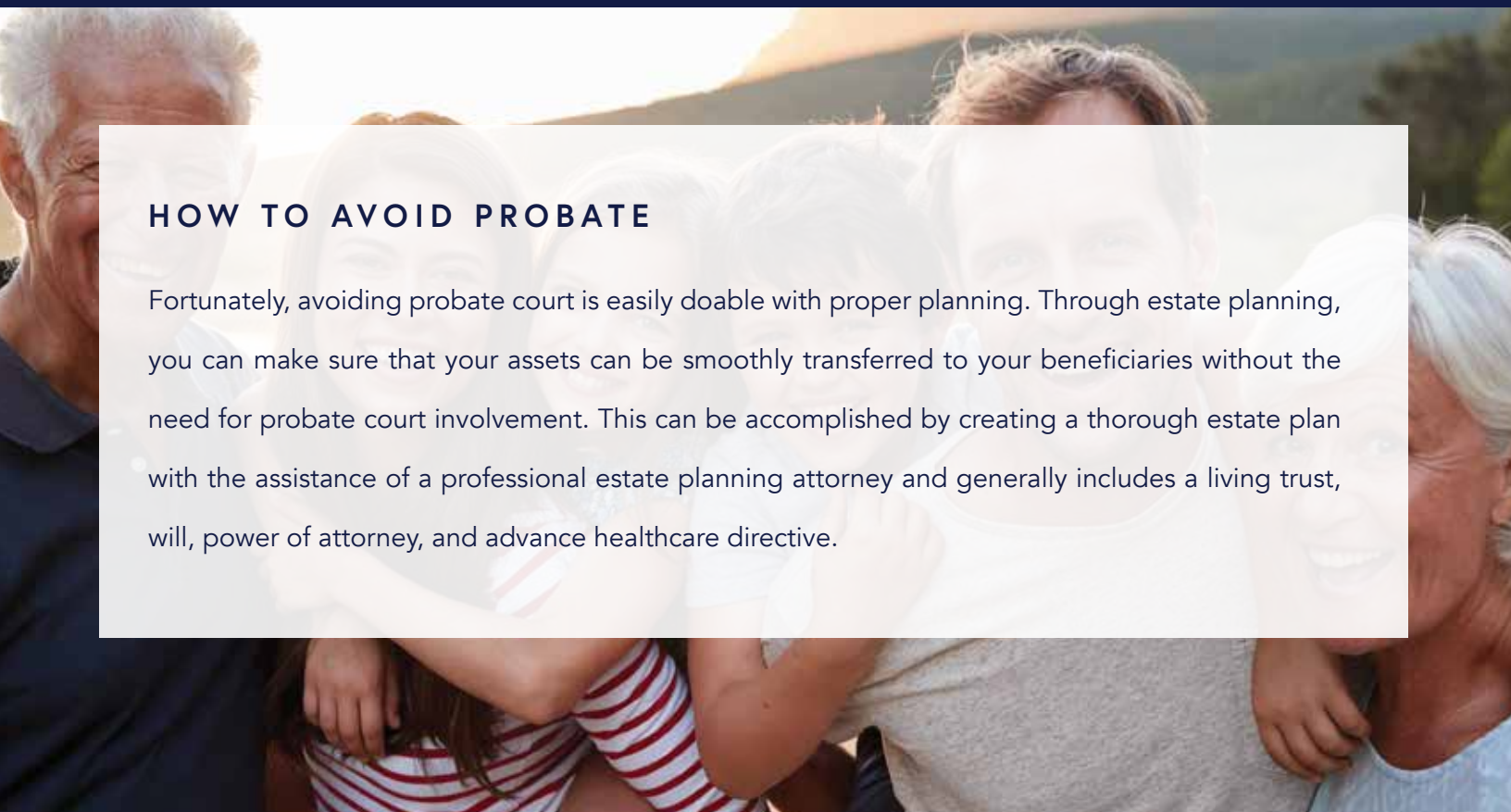
WHAT IS PROBATE ANYWAY?

Probate is a court proceeding in which the person's estate is administered and assets ultimately divided either according to their will, or if there is no will, to their heirs under California intestate succession laws. Probate is a lengthy process that involves a substantial amount of paperwork, money, and time. Notice must be given to the State and creditors to make sure that all debts and creditors are paid or addressed. In order to avoid a complex probate process and to have greater control over your assets in the future, you should take proactive steps to plan your estate (usually through a living trust).

Probate cases can be expensive and can sometimes take over a year to complete. The local courts are backlogged and do not have enough resources, so it takes a long time to get a court date. In probate cases, statutory probate attorney's fees are based off of the gross value of the estate, they are:

4% OF FIRST $100,000 OF ESTATE
3% OF SECOND $100,000 OF ESTATE
2% OF NEXT 800,000 OF ESTATE

That means that if the estate is worth $400,000, the statutory fees you would pay would be $9,000. Filing fees and miscellaneous costs (publication in a legal newspaper, etc.) would bring the total probate fees and costs up to around $11,000.



HOW TO AVOID PROBATE

Fortunately, avoiding probate court is easily doable with proper planning. Through estate planning, you can make sure that your assets can be smoothly transferred to your beneficiaries without the need for probate court involvement. This can be accomplished by creating a thorough estate plan with the assistance of a professional estate planning attorney and generally includes a living trust, will, power of attorney, and advance healthcare directive.

OTHER IMPORTANT DOCUMENTS - FINANCIAL POWER OF ATTORNEY

A Power of Attorney allows you to name someone you trust as your agent to step in to take care of you and your financial matters. Usually a power of attorney is set up to be effective only upon your incapacity - if sometime down the road you are unable to make decisions for yourself. Such situations could arise from an accident, a coma, or dementia. Alternatively, a power of attorney could be set up to be effective immediately if you wanted someone to step in and help you right away.

Bottom line, if something happens to you, you want a power of attorney set up so that nobody has to go into court to have authority to take care of you. If something happened to you today, who would be able to take care of things? Who would be to able access your financial accounts, pay your mortgage, talk to your cable company, etc.? A spouse might be in a decent position to handle most of this stuff, but there's almost always some red tape they run into. And what if your spouse is also unable to handle things?
The goal is to make sure that you are choosing the person you trust to be able to step in and take care of you, without their having to go through a lengthy court process of getting a conservatorship to get legal authority to take those same actions. Not only does this save a huge amount of time and money in avoiding court, it prevents family members from fighting each other for decision making authority. You also name backups in the document, so that if your first choice is not able to act, you have alternates lined up.

Everybody, even young adults with little to no assets, would be wise to have a power of attorney in place to address these potential situations. Even seemingly small things, like dealing with a utility or cell phone bill in someone's name alone, can be very problematic if a power of attorney is not in place.

OTHER IMPORTANT DOCUMENTS - ADVANCE HEALTHCARE DIRECTIVE

An Advance Healthcare Directive provides for a medical power of attorney similar to the power of attorney addressed above. It allows you to name someone you trust to step in as your agent to take care of you, but specifically to address health care decisions. This includes speaking to doctors, getting medical records, and generally making health care decisions should you be unable to do so.

These documents are vital to have in place, especially in the case of an unexpected emergency medical situation. It is a terrible situation to have a family member, child, or significant other run into a bureaucratic road block in getting important healthcare information because there isn't something in place. The goal is to be able to legally deal with these issues by having an advance health care directive so that nobody has to go through a lengthy and expensive court process called a conservatorship, especially considering the slow nature of such proceedings and the immediate need to make decisions in these situations.

HOW OFTEN SHOULD YOU UPDATE OR REVIEW YOUR ESTATE PLANNING DOCUMENTS?

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REVOCABLE VS. IRREVOCABLE TRUSTS

The term "living" with reference to a Living Trust simply means that you are setting it up during your lifetime. Revocable means that you can revoke it or change it while you are still alive should you want to change things in the trust down the road, such who you are putting in charge of the trust after you pass away, or who you are naming as beneficiaries. The vast majority of trusts are revocable living trusts. Irrevocable living trusts, on the other hand, restrict your ability to revoke or change your trust, and they are generally used in very specific situations to deal with special circumstances.

WHAT HAPPENS IF YOU DON'T SET UP A WILL OR TRUST

If you pass away without having a will or trust, the courts will be left to determine how your assets will be distributed. California applies its intestate succession laws to assume who you would have left as your heirs, and unfortunately, this can deviate significantly from what people would have wanted. It does not matter if you verbally tell someone your wishes, or even leave video/audio evidence of your wishes, you need a validly executed will or trust to make sure your wishes are followed.

WILL THE STATE SEIZE MY ASSETS IF I DON'T HAVE A WILL OR TRUST?

This is often a concern. The answer is generally no, at least not immediately. If you don't have proper estate planning mechanisms set up, your estate would be administered according to California's intestate succession law through probate court, and your heirs would still inherit your assets. However, if no one initiates a probate case, then some assets in your estate might be lost, properties might go into foreclosure if the mortgage isn't paid, and unclaimed financial accounts might escheat to the state until they are claimed (if they are ever claimed) through probate by your heirs. That is why it is better to make sure everything is set up to address these issues.

CAN'T I JUST ADD SOMEONE TO THE DEED ON MY HOUSE INSTEAD OF SETTING UP A TRUST? WOULDN'T THAT BE EASIER?

A Living Trust is hands down the best approach for dealing with real property. Some people take the approach of transferring assets to family members during their lifetimes, or signing a deed to put their children on title to their property. This is a bad idea, for a number of reasons:

OWNERSHIP

If you put another individual on title, then you are essentially giving away all or part of your property while you are alive. We commonly see this where a parent transfers ownership in their home to their child, with the expectation that it will only affect things once they pass away and that they will continue to be able to use the home as they have been. Unfortunately, by deeding them property and putting them on title, the child has an immediate, legal ownership interest

in the property. They could exercise control over the property freely, and potentially force the sale of the property. While such deeds are usually done with close, trusted family members, we have seen situations where there is a falling out between these family members years later. Or a significant other, daughter-in-law, or son-in-law comes into the picture suddenly and starts pressuring the child to take certain actions.

Hopefully these situations would never come up, but there's little reason for people to put themselves in these situations given the better alternative of a living trust.

EXPOSURE TO CREDITORS

By giving family members immediate ownership interest in the property, you are exposing your property to that family member's creditors. For example, if you put your son on title to property, and he has a substantial amount of debt, his creditors could sue him and go after the home. Even if he does not have debts, he could accidently cause a car accident or injure someone, which could expose him to liability. If he is sued, and there are major damages involved, the house could be put at risk. While the odds of this happening are hopefully slim, it is something that people need to be aware of.

CAPITAL GAINS TAX

One of the most compelling reasons to have a living trust is the benefit your beneficiaries can receive in terms of avoiding capital gains tax. Generally, if you sell your property while you are alive, you will be taxed on the difference between the amount you originally purchased your property for and the amount that you sell it for. For instance, if you originally purchased your property for $100,000 and you sell it for $400,000, then the $300,000 increase in value could be subject to Capital Gains Tax.

When you transfer ownership to a family member, their basis for capital gains tax purposes is the value of the property as of the date of the transfer. For instance, if your child inherits property valued at $400,000 through a trust when you pass away, then their basis is $400,000. That means that if they sell it shortly after you pass away, there are ZERO capital gains. This can mean massive tax savings!

If they hold onto it and sell it for $450,000 years down the road, then only that $50,000 is subject to capital gains, instead of $350,000 in capital gains.

So why does this mean that living trusts are better than putting a child on title? Since property values traditionally go up as time goes on, it is better to have that transfer occur later in time. If Mom put Son on title through a deed when the property was worth $100,000, then the son's basis will $100,000. If he sells the property when mom passes away years later when the house is worth $400,000, he will be stuck dealing with $300,000 in potential capital gains tax. This can come as a terrible surprise in these situations. A Living Trust avoids this.

I'M MARRIED, DOESN'T EVERYTHING I OWN JUST GO TO MY SPOUSE UPON DEATH?

No, and unfortunately, this is a common mistake. Sometimes it works out. If a home is held as joint tenants or as community property with right of survivorship, and all other financial assets are held jointly in both spouse's names, then this isn't generally a problem if one spouse passes away. The surviving spouse will be the sole owner and will be able to deal with the assets.

However, for any assets in one spouse's name alone, the surviving spouse will be unable to deal with that asset without going through a probate procedure unless there is some estate planning mechanism set up for them to inherit the asset.

We see this on a regular basis when a married couple refinances a property, and the property and loan is put in one spouse's name alone. This can create a huge headache if that named spouse passes away. We have to go into probate court to transfer the property to the surviving spouse, and in some situations, a child or children might claim an interest in the property at that time.

Financial assets held in one spouse's name alone might be easier to deal with, but depending on the size of the assets and the situation, we may end up in probate court in a similar situation. That being said, it is worth the time to make sure things are set up properly to avoid these legal hardships at a time when a spouse is normally grieving. At the very least, you will likely want to set up some minimal estate planning to also cover in the case that one spouse is incapacitated and unable to make decisions.

IF I DON'T DO ANYTHING, WILL PROBATE BE ABSOLUTELY NECESSARY?

There are many cases in which we are contacted by family members after or close to the death of a loved one. In these situations, it is usually too late to set up a living trust or do any type of estate planning. While this may ultimately necessitate filing a probate case, there are some cases in which a full blown probate case may not be necessary.

There are some alternatives to probate in California, and your family qualifying for those alternatives depends on the value of the estate and the kind of assets in the estate. This can largely depend on whether the estate is considered a small estate. Given the values of homes in California, most cases involving a home without a trust will require going through probate, regardless of whether there is a mortgage or not.

Oftentimes probate is the only way, but it is important to speak to an attorney before taking action to determine if you qualify. Our firm has a separate e-book dedicated to addressing these probate alternatives which we can provide upon request.

In any event, these alternatives serve more as damage control instead of recommended planning. While not as burdensome as a normal probate case, these alternatives can be expensive and time consuming, so it is best to set up your estate plan to avoid the possibility of probate entirely.

FOR MORE INFORMATION ABOUT STARTING YOUR ESTATE PLAN, SCHEDULE A FREE INITIAL CONSULTATION WITH THE WERNER LAW FIRM TODAY.

ABOUT THE AUTHOR

Troy Werner has been an indispensable asset to The Werner Law Firm since joining in 2009, providing exceptional legal service to its clients. An Ivy League graduate, he has won numerous awards during his tenure as an attorney, including being recognized with an award as one of the top 40 individuals under 40 in the community. His goal is to help give clients peace of mind in dealing with their individual legal situations. In collaboration with his father/founder of the firm, L. Rob Werner, and backed by the firm's dedicated and experienced team of attorneys and legal professionals, he plans to continue the firm's tradition of excellence well into the future.

Education:

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