

WILLS
VS.
REVOCABLE LIVING TRUSTS

What's the difference?

Oregon Humane Society

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I. INTRODUCTION.¹

- A. The analysis involved in choosing a Will or a Trust as the primary estate planning document depends primarily on the individual factors of each client.
 - 1. The first step of any individual or couple seeking to decide how to approach their estate planning documentation is to use their own individual circumstances and desires to make that decision.
 - 2. Doing this puts the horse in front of the cart and allows an experienced estate planner to assist the client in picking the document and approach best suited for each client's circumstance.

II. WHY DO WE CARE?

- 1. To assist the estate planner, and ourselves, in determining the best estate planning document format, it is important to identify what is most important to us:
 - a. Effectiveness of the document
 - b. Ease of administration:
 - c. Creation of the documents
 - d. Operation of the documents
- B. Probate issues.
 - 1. Is probate something that is important to be avoided? Is it that big a deal?
 - 2. Are there benefits to probate that should be taken advantage of?
- C. Who's selling what?
 - 1. Many times, trusts, or other complex estate planning devices are utilized by companies or individuals selling a product, such as life insurance, annuities or other techniques which may or may not be well suited to each client's needs.
- D. What is most important to you? What do you care about most?
 - 1. Access to you funds
 - 2. Ease of access to funds if you are disabled or incapacitated

¹ References to ORS are to the Oregon Revised Statutes.

3. Ease of distribution to heirs
4. Avoiding disputes among heirs
5. Making sure all creditors or debts are paid – avoiding claims against beneficiaries of your estate.

III. METHODS OF TRANSFERRING PROPERTY AT DEATH.

- A. Operation of Law.
- B. Will/Probate.
- C. Revocable Living Trust.
- D. Alternatives for Small Estates.

IV. WHAT IS A WILL?

- A. A Will is a written document controlled by state law. The Will's effect is to control the disposition of the Will-maker's (known as a "testator") assets.
- B. In Oregon, a Will has to satisfy certain formalities. Those formalities can vary from state to state. In Oregon, ORS 112.225 – 112.435 governs the formalities of a Will.
- C. Oregon Will formalities are as follows:
 1. A written document
 2. Witnessed by two witnesses. ORS 112.235
 3. In Oregon, un-witnessed Wills are non-binding.
- D. A Will is not official and does not come into effect until after the testator dies and a probate proceeding is filed to confirm the validity of the will and appoint the executor (known in Oregon as the Personal Representative).
- E. It is important to have a qualified attorney prepare a Will.
 1. Document preparation services, paralegal services and internet sites often provide documents that may be unsuited to the client's needs, do not contain all the necessary provisions or are simply inadequate.
 2. For example, selecting backups for guardians, trustees or others named in the Will.

- F. If a person dies without a Will, property does not automatically go to the state. Instead, the rules of “intestate succession” control, on a state-by-state basis. In Oregon, the intestate succession rules are found in ORS 112.015 – 112.115.
 - 1. The intestate succession rules generally provide that the heirs of the decedent inherit in order: first the surviving spouse, then the children, and so on.
 - 2. Problems arise because of second marriages with children from first and second marriage. Often, surprising results can occur. For example, where there is a surviving spouse, but children from a former spouse, the estate is divided half to the surviving spouse and half to the children from the first marriage.
- G. Note that a Will has no management value during the client’s lifetime.
- H. Upon a person’s death, the provisions of the Will control the distribution of assets that flow through the estate.

V. **UNDERSTANDING PROBATE.** Probate is a procedure through which the court supervises the distribution of a decedent’s property. The probate process is as follows:

- A. A petition is filed submitting the decedent’s Will to probate (or stating that the decedent died without a Will) and asking the court to appoint a personal representative. The court-appointed personal representative receives Letters Testamentary.
- B. A notice to creditors identifying the personal representative and the attorney for the personal representative is published in a county paper of general circulation (Daily Journal of Commerce) for three (3) consecutive weeks. Creditors have four (4) months to submit claims to the personal representative.
- C. Creditors who are known to or reasonably ascertained by the personal representative must be mailed a notice of the period in which to file claims.
- D. Heirs are notified of the filing of the probate proceeding.
- E. The personal representative collects assets of the decedent and files an inventory of the decedent’s assets with the court.
- F. The personal representative has the authority - and duty - to oversee and protect the decedent’s assets and accounts.
- G. After the four-month period for creditors to file claims expires; the personal representative pays valid creditor claims.
- H. The personal representative is responsible to file the appropriate state and federal tax returns for the decedent and the estate.

- I. The personal representative distributes property to the beneficiaries and closes the probate.
- J. The personal representative is entitled to a statutory fee based on a percentage of the value of the estate.
- K. In Oregon, attorney fees are based on actual time spent by the attorney and must be approved by the court.

VI. LENGTH OF PROBATE. These are only estimates and can vary widely depending on the county in which the probate is filed and on the estate's assets and beneficiaries.

- A. Simple Estate. Six to ten months.
- B. Complex Estate. Twelve (12) to twenty-four (24) months or more.

VII. ADVANTAGES OF PROBATE.

- A. Cuts off claims of creditors (important for professionals).
- B. Establishes values of appreciated property for estate and income tax purposes.
- C. Personal representative's activities are court supervised to ensure proper distribution of the decedent's assets.

VIII. DISADVANTAGES OF PROBATE.

- A. Probate files are public record.
- B. Costs such as court fees, attorney's fees, accounting fees and personal representative's fees.
- C. Delay of at least six months and possible more.
- D. Real property owned by a decedent in a different state will require an ancillary probate in that state.

IX. OTHER ASSETS NOT CONTROLLED BY THE WILL:

- A. Certain types of ownership will pass outside of Probate and will not be controlled by a Will (or Trust):
 - 1. Joint tenancy accounts

2. Retirement plan beneficiary designations
 3. Life insurance beneficiary designation
 4. Pay-on-death (POD) accounts
 5. Transfer-on-death (TOD) accounts
- B. The use of probate avoidance devices cited above can be effective but can also adversely impact the ability to do tax planning using a Will.
- C. Ownership of real property in another state can also complicate the distribution process. This is because real property owned in another state (including drilling rights, or other mineral rights) will require an “ancillary probate” in that other state.
- D. For estates with less than \$75,000 in personal property and \$200,000 in real property (gross fair market value), a simplified probate process is available, called a “Small Estate Affidavit”.
1. It is surprising how few estates fall into this category.
 2. This process will not allow the sale of real property without other steps.
- E. A Will can establish a Trust inside of it to provide for heirs or minors who cannot otherwise inherit or would not do well directly inheriting. This is known as a “Testamentary Trust” and is often used to provide for minor children or tax planning.
- F. To amend a Will, it is necessary to execute a document called a “codicil”. A codicil must be signed using the same formalities as a Will (two witnesses, etc.).

VI. REVOCABLE LIVING TRUSTS

- A. A trust is a relationship established when party (a “Trustor” or “Settlor”) transfers property to a second party (a “Trustee”) who must use the property solely for the benefit of a third party (a “Beneficiary”). The Trustor, Trustee and Beneficiary may be all the same person, or may all be different persons.
- B. Because the trust – when properly funded – owns the property, the death of the Trustor or Trustee has no effect on ownership.
1. When the Trustor dies, the trust becomes irrevocable.
 2. If the Trustee dies, the successor Trustee named in the Trust instrument takes over. If no successor is named, one can be appointed.

- C. Trusts are generally more complex than Wills, because while a Will only governs what happens after death, a Trust must cover three circumstances:
 - 1. Management during the Trustor's lifetime;
 - 2. Management during the Trustor's incapacity; and
 - 3. Management after the Trustor's death.

- B. Trusts, unlike Wills, are generally not subject to the probate process, if properly funded. The operation of a Trust, absent problems, is generally not overseen by the court.

- C. Let's spend a moment on the advantages and disadvantages of a Revocable Living Trust:
 - 1. Advantages:
 - a. Management.
 - i. Properly funded, all investment and real property assets are in one entity. Much easier to review and manage.
 - ii. This is especially true if real estate is owned in another state:
 - A. E.g., a vacation home in Palm Springs or Arizona.
 - B. This avoids the requirement of an ancillary probate in the foreign state for that property.
 - b. Disability protection.
 - i. If the Trustor, the initial trustee, becomes incapacitated, the successor Trustee named in the document takes over without any court intervention.
 - A. The successor Trustee has full power over the Trust's assets.
 - B. Much broader powers than a durable power of attorney.
 - C. A successor trustee is better recognized by brokerage houses, custodians and banks and as having that power, as compared to an agent named under a durable power of attorney.
 - 1. This avoids problems with financial institutions that sometimes refuse to recognize a durable power of attorney.
 - c. Adaptability.

- i. The Trust is completely flexible and can be amended or even revoked by the Trustor during their lifetime.
 - ii. Easy to revise in light of changing circumstances.
 - d. Can help reduce the risk of a Will contest by uncooperative family members because there is no probate providing a forum for the contest.
 - e. Less delay in administration.
 - i. Often cited as the key reason for the use of an RLT, a court procedure in the form of a probate does not exist, thus speeding the administration of the trust after death.
 - ii. After the Trustor's death, the Trustee is free to pay bills, liquidate assets and distribute them without court involvement.
 - iii. Compare to a probate estate:
 - A. At least six months' delay – including a four-month creditor notice period.
 - B. The requirement, in Oregon, of court approval for distributions.
2. Disadvantages:
- a. Cost. Because the RLT does so much more, more time is spent in drafting it. This translates to a greater cost than a Will.
 - b. Funding.
 - i. The Trustor's important assets – including investment accounts, real property, business interests, time shares and the like – must be transferred into the name of the Trust.
 - ii. Failure to do so, or leaving out an important asset, will require probate for unincluded assets.
 - iii. Failing to fund an RLT is the most common reason they fail.
 - c. Increased attorney fees, accounting fees and Trustee's fees; costs in funding Trust at creation.
 - d. Does not reduce estate or income taxes.
 - e. May not avoid probate if trust is not properly funded.

- f. No protection from claims of creditors.
- D. The key to the effective use of a living Trust is to fund it.
- 1. Funding means transferring assets into the name of the Trust.
 - 2. This is the one area where most Trusts fail: failure to properly fund the Trust.
 - 3. Failure to properly fund a trust means that the assets remain in the name of the trust maker, and therefor, on death, are not governed by the Trust.
 - 4. Most “do-it-yourself”, paralegal document preparation, and internet providers of living trusts fail to follow up properly on Trust funding. This is where most of these products and mass-market purveyors fail.
- E. Remember that assets subject to beneficiary designations (retirement accounts, 401k, IRA, life insurance) and assets governed by pay-on-death or transfer-on-death designations, as well as joint accounts will not be subject to a Trust’s provisions, because those assets are transferred by operation of law or by the beneficiary designations.
- 1. However, a Trust can be made the beneficiary of life insurance, bank accounts, etc.
- F. **BE VERY CAREFUL ABOUT DESIGNATING A TRUST AS THE BENEFICIARY OF AN IRA ACCOUNT OR RETIREMENT BENEFIT.**
- 1. In light of changes made by the SECURE Act, passed by Congress in December 2019, you must consult competent tax and legal counsel to determine which is best for you. Failure to do so could result in potentially disastrous tax consequences to your heirs.
- G. The selection of a successor trustee is very important.
- 1. A family member may be an obvious choice, but not the best one.
 - 2. A professional trustee may be a better choice
 - 3. Picking backup successor trustees will be important to make sure you are fully covered if your first successor trustee cannot act.
 - 4. Consider the use of a trust protector, who is a person to oversee the acts of the successor trustee and replace that trustee if necessary.

VII. LET'S COMPARE WILLS VS. TRUSTS

- A. Note that Wills and Trusts are two different mechanisms to accomplish the same goal: what happens to my assets on my death, who gets them, and how.
- B. Deciding whether a Will or a Trust is better for you depends upon how you analyze the different advantages and disadvantages of each approach.
- C. Trusts can be effective (whether living Trusts or testamentary) for the following reasons:
 - a. Provide for a spouse, children or other dependants
 - b. Providing tax planning
 - c. Ensuring that upon the death of a spouse, that remaining assets will go to the couple's children, not to the second spouse or others.
 - d. Providing tax and asset protection for heirs
 - e. Keeping assets away from heirs until they reach certain ages
 - f. Providing instructions that encourage certain behaviors (such as a Trust for educational purposes, etc.)

VIII. CONCLUSION

- A. Generally, Wills are going to be cheaper up front and easier for clients, since they don't require asset transfers - the "funding" of the Trust.
- B. The administration of a probate estate creates more complexity and expense later.
- C. Revocable Living Trusts, on the other hand, are more expense and work up front, but usually require less complication and delay later.
 - 1. That is, Trusts are front-loaded in expense and complexity, while Wills are back-loaded with expense, complexity and delay.
- D. The best way to answer these questions to determine whether a Will or Revocable Living Trust is better for you, is to answer these questions: At death:
 - 1. What you want to have happen?
 - 2. How you want your assets distributed?
 - 3. How you want your heirs to inherit them?

Answering these questions first will allow your estate planning professional to give you the best advice, for the best result based on your and your heirs' individual circumstances.

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