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NebFact



Published by Cooperative Extension, Institute of Agriculture and Natural Resources,
University of Nebraska-Lincoln

A Trust as an Estate Planning Tool

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This is one in a series of **NebFacts** providing information on the use of estate planning "tools" — mechanisms that can be used in attaining desired estate planning outcomes. Titles in the series are listed following the last narrative section of each document. Reading the documents in this series will improve your understanding of estate planning tools and alternatives, and make it easier to communicate with your attorney, accountant, and other helpers when your estate plan is prepared.

Your need for legal and tax advice: While the information contained in this document is thought to be accurate, it should not be used as a substitute for legal advice on matters related to business organization, taxation, estate planning, gifting of assets, life insurance, or other business and financial management matters. Consult with your legal and tax advisers before making decisions.

What is a Trust?

A trust is a legal mechanism that separates the responsibility of owning property from the benefits of owning property. A trust is established by a grantor or grantors — the person or persons owning property to be placed in the trust. Property placed in the trust is called the corpus of the trust. The corpus can include part or all of the property owned by the grantor(s).

The nature of the trust is identified in a document called a trust instrument or trust declaration. By whichever name — trust instrument or trust declaration — the trust document identifies the trustee and describes the powers given to the trustee, who can be a person or a business (for example, a bank), or another entity. The trustee receives the property, places it in the trust, and manages the trust for the benefit of a beneficiary or beneficiaries as identified in the trust declaration.

Instructions for distributing the trust income and the corpus of the trust, whether this distribution is to occur during the life of the trust or upon its termination, are included in the trust declaration. If stipulated in the trust declaration, the trust's income beneficiaries also can receive distributions of the trust property (the corpus).

Trusts created during the lifetime of the grantor are called living trusts and are of two types: (1) revocable trusts can be modified and assets can be moved into or out of the trust during the grantor's lifetime (the grantor can be, but need not be, the trustee); and (2) irrevocable trusts that cannot be altered after being established. Upon the death of the grantor, a revocable trust becomes irrevocable.

A testamentary trust is created after the grantor's death under the provisions of his or her will — the nature of the trust declaration is specified in the will. By the nature of its creation, a testamentary trust is irrevocable. A testamentary trust will not be created if the will is revoked prior to the death of the testator (the person who writes or has written and signs a will), or if the will is not recognized as valid when submitted for probate.

Trusts usually are established for a designated period of time, or until specified actions are taken or events occur. For example, a trust can be established to exist until a beneficiary is married or reaches a specified age, until a beneficiary's death, until the grantor's death, or until some other specified event occurs.

What property is included in a typical trust?

A grantor can place almost any type of tangible or intangible property in a trust. A farm or ranch, most stocks and bonds, a business firm, money, savings bonds, certificates of deposit, a patent or copyright — all are property that can be placed in a trust.

After property is placed in a trust, it is owned by the trust. The trustee is responsible for investing capital, buying and selling assets, receiving income, and taking other actions consistent with the authorizations and instructions in the trust declaration. The trustee must avoid conflicts of interest in the investment and management of trust property. Without regard to the nature of property placed in a trust, the trustee has a duty to take possession of it, to invest or manage it in a profitable and business-like manner, and to preserve it from loss or damage. The trustee is required to keep complete and accurate records of all trust activities. All distributions from the trust must be in accordance with instructions contained in the trust declaration.

How is a trust used in estate planning?

In estate planning, trusts are used in several ways. Frequent uses include:

- as a means of protecting assets, providing income and financial management services, and distributing to beneficiaries the assets of persons who prefer not to, or are unable to care for and to manage their property;
- as a means of avoiding federal and state taxation when married couples have assets valued at more than \$600,000 by placing part or all of the assets of the "first to die" in a trust for the benefit of the surviving spouse during the remainder of his or her life; following the death of the surviving spouse, the trust assets are distributed to surviving beneficiaries in accordance with instructions in the trust declaration;
- as a means of protecting assets of a decedent while providing income for minor children
- as a means of protecting an inheritance and providing income for a person who is incapable of appropriately owning and managing the inheritance;
- as a means of meeting any specialized management needs resulting from the nature or complexity of assets held by the grantor(s);
- as a means of avoiding probate of the estate and its public disclosure of the nature and value of assets owned by the decedent;

- as a means of attaining other estate planning objectives of importance to the grantor(s).

Discussion with a bank trust officer and/or with an attorney who specializes in estate planning is a good way of becoming more fully informed on trusts. Articles in financial management magazines, or information in books available in most public libraries and bookstores also can provide you with information on using a trust as a means of implementing your estate plan.

Can a trust be my only estate planning tool?

Trusts generally are used in combination with other estate planning tools. The grantor of a trust should have a valid and current will to ensure that all aspects of an estate plan can be implemented when needed. Depending on the size and complexity of your estate, you may find that other estate planning tools used in conjunction with a trust will improve your ability to attain your estate planning goals.

It's important also to keep in mind that there are interactions between the form of business organization of your business and your ability to use a trust for some estate planning purposes. For example, a trust usually can hold S Corporation stock for only a brief time following the death of the owner of the stock.

In any case where you are considering using a trust as an estate planning tool, you should seek legal advice very early in your estate planning activities to ensure that you understand the possibilities and limitations of using a trust in your situation.

What are income tax consequences of using a trust?

Under some circumstances, the tax liability on trust income can be greater than the tax liability on the same amount of income reported on the personal income tax return of the grantor or the beneficiary. Keep in mind that placing property in a trust can result in increased income tax liabilities unless the trust income is distributed to the beneficiaries in ways that avoid it being subject to taxation as trust income. If you are thinking of establishing a trust to implement one or more aspects of your estate plan, consult your tax advisor before making your estate planning decisions.

Should I use a trust in my estate planning?

Depending on circumstances, it may be desirable for your estate plan to include establishing a trust. Here are several circumstances where a trust may be useful:

- if you have minor children, or if your intended heirs will need assistance in managing assets and finances, you may want to consider establishing a trust;
- if you have no close relatives living near you, or if you believe it would be a good plan to have someone other than your relatives manage your property during the final years of your life, you may want to examine trust alternatives;
- if you and your spouse have accumulated property with a total value greater than \$600,000, it may be that establishing a trust with the surviving spouse as the income beneficiary and intended heirs as ultimate recipients of trust assets could reduce legal and estate tax costs of succession;
- if you own property located in another state that will be subject to a probate process there, it may reduce costs and delays to place the property in a trust and avoid probate in that state;
- if you have property that requires a type of management that you believe can best be provided by a professional manager acting as trustee, it may be best to place it in a trust;
- if you believe that placing your property in a trust would reduce the chances of future family conflicts, you may want to consider placing your property in a trust.

Overall, there is no "Yes" or "No" answer to "Should I establish a trust . . ." The answer depends on your circumstances, the outcomes you want to attain, your insights about the circumstances and characteristics of your intended heirs, and the availability of persons who can manage your affairs when you are unable to do so yourself. It's important to seek advice from persons skilled in estate planning and tax management before deciding whether establishing a trust will help you attain the management and succession outcomes you believe are most desirable.

Glossary:

Beneficiary

A person who receives income or assets from a trust — a person who benefits from the existence and operations of a trust.

Corpus of a trust

Term used to designate the body of assets (property) placed in a trust. The trust holds title to all property included in the corpus.

Grantor

The person placing property in a trust.

Irrevocable trust

A trust that cannot be changed after it is established.

Living trust

A trust established during the lifetime of the grantor.

Revocable trust

A trust that can be changed after it is established. Assets can be added or removed from the corpus of the trust, the beneficiary(ies) can be changed, and other changes including termination of the trust, are allowed. A revocable trust becomes irrevocable upon the death of the grantor.

Testamentary trust

A trust established after the death of the grantor under the provisions of the grantor's will.

Trust

A legal mechanism that separates the responsibility of owning property from the benefits of owning property. Property placed in a trust is owned by the trust, and no longer is owned by the grantor(s).

Trust declaration or trust instrument

A document defining the nature and duration of the trust, the powers of the trustee, and identifying the trust's beneficiary(ies).

Trustee

The person or legal entity such as a bank or trust company who receives property and places it in a trust, and manages the trust for the benefit of the beneficiary or beneficiaries in ways consistent with the trust declaration and good business practice.

Documents in This Series:

- NF 95-236, *Nebraska Inheritance and Estate Taxes*
- NF 96-291, *Intestate Succession As An Estate Planning Tool*
- NF 96-291, *A Will As An Estate Planning Tool*
- NF 96-293, *Joint Tenancy As An Estate Planning Tool*
- NF 96-294, *Tenants In Common Ownership As An Estate Planning Tool*
- NF 96-296, *Gifting As An Estate Planning Tool*
- NF 96-297, *Life Insurance As An Estate Planning Tool*
- NF 96-298, *Charitable Remainder Trusts and Charitable Annuities As Estate Planning Tools*

- NF 96-299, *Estate Planning Glossary*

File NF295 under: HOME MANAGEMENT

B-8e, Estate Planning

Issued October 1996

Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture. Elbert C. Dickey, Director of Cooperative Extension, University of Nebraska, Institute of Agriculture and Natural Resources.

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