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Misconceptions of a Revocable Living Trust

A revocable living trust, or RLT, offers many benefits, including probate avoidance, privacy, and flexibility in managing assets during one's life, incapacity, and death. However, despite their popularity as an estate planning tool, there are many misconceptions surrounding revocable trusts that lead to confusion and misunderstandings.

In this document, we'll explore six common misconceptions to help you better understand how revocable living trusts operate.

#1 Myth:
Revocable trusts are only for the wealthy

One of the most common myths is that trusts are only for the wealthy. While there are many types of trusts and estate planning strategies, RLTs can be a practical tool for virtually anyone.

An RLT enables you to maintain control over your assets during your lifetime. If you become incapacitated or pass away, the trust can continue to manage those assets via a successor trustee of your choice.

If properly funded, an RLT can allow your assets to bypass the probate process. While each state has its own rules, costs, and procedures, the probate process can often be time-consuming and costly. Also, many assets you leave behind may only be available to your heirs once the probate process is complete, which can take several months to years.

An RLT can also provide privacy for you and your heirs. Unlike a Will, which becomes part of the public record, an RLT is a private document that does not need to be filed with the court. This can be especially beneficial if you have complicated family dynamics or want to keep your financial affairs private.

#2 Myth:
Revocable trusts offer protection from creditors and lawsuits

Another common misconception is that revocable living trusts offer protection from creditors and lawsuits. While an RLT can provide many benefits, protection from creditors is not one of them. This is because RLTs are designed to be flexible and revocable - meaning you can change the trust at any time, and you have full control over the assets in the trust. Because you retain dominion and control over the assets, they are still considered part of your estate for creditor and liability purposes. If you are sued, creditors may be able to go after the assets in the trust just as they would if the assets were in your name.

With that said, there are other types of trusts and business structures that can offer creditor and asset protection. For example, irrevocable trusts can help protect assets by separating the assets from their original owner and placing them under the control of a separate trustee.

#3 Myth:
Revocable trusts are the same as a Will

Another misconception is that RLTs are the same as a Will. While both documents are part of estate planning and can be used to distribute assets after death, they serve different purposes and provide different benefits.

A Will can outline your wishes for the distribution of assets after your death and identify an executor who would be responsible for carrying out those wishes, name guardians for any minor children and include provisions for funeral arrangements.

A Will is a public document, and most assets listed for distribution as part of one's Will are subject to the probate process. A Will also does not apply during incapacitation and only comes into effect after one's passing.

A revocable living trust can also outline your wishes for the distribution of your assets. However, it can allow for your assets to be distributed to beneficiaries during your life, incapacity, or after death. It typically does not include provisions for guardianship of minor children or funeral arrangements. Unlike a Will, an RLT is not a public document and assets properly titled in the name of your RLT are not subject to probate.

#4 Myth:
Revocable trusts require you to give up control of your assets

There is a misconception that RLTs require you to give up control of your assets. While this is true of irrevocable trusts, one of the primary benefits of a revocable living trust is that it allows you to retain control of your assets during your lifetime. You can buy and sell assets, add or remove assets from the trust, and even revoke the trust entirely if you choose to do so.

#5 Myth:
I would have to file a separate tax return for the trust

Another misconception is that you have to file a separate tax return. A benefit of a revocable living trust is that it does not require filing a separate tax return. Instead, the trust uses the grantor's social security number, and any income generated by the trust is reported on the grantor's personal tax return. Likewise, assets in the trust may still be subject to estate taxes if they exceed certain thresholds when the grantor passes away.

Once the grantor passes away (or both grantors, in the case of a spousal living trust), the successor trustee will need to obtain a tax identification number for the trust and file a separate tax return. This is because the trust becomes a separate legal entity after the grantor's death, and any income generated by the trust will need to be reported and paid by the trust itself.

#6 Myth:
I would have to pay trustee fees

Another common misconception about living trusts is that they require trustee fees, which can be costly and eat away at the trust's assets. However, this is not necessarily true. When you establish a revocable trust, you are typically the initial trustee and do not need to pay any fees to yourself.

If you name a successor trustee to take over your trust after your death or incapacity, they may receive compensation for their services. However, the amount and frequency of these fees can be stipulated within your trust. In many cases, the successor trustee is a family member who is willing to serve without compensation.

Final Thoughts

This document is intended to provide a brief overview of common misconceptions about revocable living trusts and is not a substitute for speaking with one of our expert advisors. If you would have questions or would like to discuss your estate planning with one of our advisors, please contact our office.

About Harding, Shymanski & Co.

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