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THE LIVING TRUST

This explanation has been prepared to give you a general idea of what a "Living Trust" is and how it works, and some of the advantages and disadvantages of using it. I hope you will find it useful.

You should understand, however, that this is not intended as specific advice on any particular estate planning situation. Estate planning problems are unique with each person and family and the advice and documents must be tailored to meet your particular situation.

1. DEFINITIONS

a. Trust:

This is a legal arrangement under which a person known as a "trustor" or "grantor" transfers legal title to all or some of the trustor's assets to a "Trustee" to be managed under a Trust Agreement. The assets are known as the "Trust Estate" and are to be used for the benefit of the "Beneficiary" for so long as the Trust Agreement is in effect. The Trustor has the legal power to enforce the provisions of the Trust Agreement.

b. Trustor:

This is the one or more persons (such as husband and wife) who transfer the legal title to their assets to a Trustee to be managed under a Trust Agreement. Usually the Trustor or Trustors are the initial beneficiaries of the Trust. Upon the passing away of the single Trustor, or of the survivor of the two Trustors, there can be other beneficiaries such as children, grandchildren, other relatives, charities and so on.

c. Trustee:

This is the person who is the "business manager" of the trust and is responsible to invest, manage and distribute the assets of the Trust. A Trustee may be the Trustor or some other person, or may be a bank with legal authority to be a Trustee.

d. Beneficiary:

This is the person or persons obtaining benefits from the trust. The beneficiary (who is usually initially the Trustor) may receive income, such as payments of interest, from the assets in the Trust, and may also receive portions or all of the principal. Usually the Trustor (if a single person) or the Trustors (husband and wife, for instance) are the initial beneficiaries under the Trust Agreement. Upon the passing away of the single Trustor, or of the survivor of the two Trustors, there can be other beneficiaries such as children, grandchildren, other relatives, charities and so on, who can continue to receive protection from the Trust, or at that time the assets in the Trust can, all or in part, be distributed to the beneficiaries.

e. Trust Estate:

This is the total of the assets which have been transferred by the Trustor to the Trustee for management under the Trust Agreement. These assets may be almost any type of property, including bank accounts, certificates of deposit, stocks, bonds, jewelry, furniture, vehicles and so on. The assets also may be real property, such as a home, farm, ranch, or a rental or commercial property.

f. Trust Agreement:

This is a written contract signed by the Trustor, who is creating the Trust, and the Trustee as the person responsible for management of the Trust Estate. It includes a list of the assets making up the Trust Estate, and sets forth how the assets are to be administered and eventually distributed upon the passing away of the Trustor or the survivor of two Trustors.

g. Successor Trustee;

If the initial Trustee named in the Trust Agreement is ever unable or unwilling to serve as Trustee, there is a Successor Trustee appointed as provided in the Trust Agreement. For example, a husband and wife might be the trustor, with one of them serving as the initial Trustee (although both can so serve if they desire). Upon one spouse no longer being able or willing to be Trustee, the other spouse can be the Successor Trustee. Generally speaking, any person, such as a child of the Trustor, can be a Successor Trustee, or the Successor Trustee can be a bank. (Any bank must be authorized by law to serve as a Trustee or Successor Trustee, and not all banks are empowered to do this.)

2. ADVANTAGES OF A LIVING TRUST

a. Financial Assistance:

(1) The Trustee is to act in a "fiduciary" capacity in managing the assets of the Trust for the protection of the beneficiaries of the Trust. Generally speaking, the Trustee is required to exercise a high degree of care in administering the Trust.

(2) The Trustee is usually required under the Trust agreement to provide annual or more frequent accountings to the beneficiaries of the Trust. The Trustee may also be required to post a bond to

protect the beneficiaries in case of loss or theft of the Trust assets.

(3) As mentioned above, the Trustor is often the initial Trustee and then if the Trustor is unable or unwilling to so serve, due to illness, old age or the like, a Successor Trustee can assume the work of the Trustee.

b. Avoidance of Probate:

(1) Probate is a legal proceeding filed with and under the ultimate control of the Circuit Court. In this proceeding the expenses of funeral, last illness, and other obligations of the deceased person are paid and then a decree or order of the court is obtained requiring the distribution of the remaining assets to the beneficiaries entitled to receive the same under the Last Will and Testament of the deceased person. If the decedent left no Will, then the assets are distributed by what is called the "law of intestate succession" which provides the assets go to the surviving spouse, children and, if there are none of the foregoing, other relatives.

(2) Since the Trustor has transferred title to the Trustor's assets to the Trustee under the Trust Agreement, the Trustor no longer owns these assets in his or her name. When the Trustor passes away there is no need to have a probate proceeding to transfer the assets on death to anyone else, such as a surviving spouse, children, and so on. (The Trust Agreement provides for such distribution of assets and in this sense the Trust Agreement serves very much like a Last Will and Testament.)

(3) The Trust Agreement requires the funeral costs, expenses of last illness, taxes and other obligations of the deceased Trustor to be paid, and then that distribution be made of the assets to children and so on. Also, all or part of the assets can continue to be managed for the benefit of various persons for an extended time, such as to support a child of the Trustor, fund college education and the like. Eventually, as set forth in the Trust Agreement, the assets are distributed to persons entitled to the assets.

(4) The costs of probate can be considerable. For instance, the probate is managed by a Personal Representative (Executor) whose fee is provided by law at $1,630 of the first $50,000 in assets in the estate and 2% of all assets above that amount. (As an example, a net estate of $300,000 would require a Personal Representatives fee $6,630.) Attorney's fees to process a probate are not fixed by law, but often are approximately one-half that of the Personal Representative. However, the Personal Representative's fee is taxed as ordinary income to the Personal Representative and often the Personal Representative is a relative who does not take a fee.

(5) Probate laws require certain steps to be taken, including a four month period for creditors to submit claims, and often the processing of a probate proceeding can take six to eight months or more.

(6) Being a legal proceeding filed in court, matters pertaining to the estate, such as a listing of assets and who is to receive what, are a public record open for inspection by anyone.

(7) Under a Trust Agreement, an attorney's work is limited and the distribution of assets is less time consuming. The payment of the decedent's obligations, the nature and worth of the decedent's

assets, and the beneficiaries to receive the assets are not a matter of public record.

(8) Federal Estate taxes are imposed on estates exceeding the estate tax exemption in net value after the payment of the decedent's obligations and expenses of estate administration. The use of a Trust does not, without special provisions, avoid the requirement to pay estate taxes. (*See page 9)*

3. BASIC ELEMENTS OF THE LIVING TRUST

a. Why is it called a "living" trust?

This type of trust is called a "living trust" because it is created during the life of the Trustor when he or she signs the Trust Agreement. (It is also sometimes called an "intervivos" or "grantor" trust.) The foregoing is distinguished from a Trust created in a Last Will and Testament which is called a "testamentary trust."

b. How is the Trustor protected under a living trust?

(1) The Trustor is often the initial beneficiary under the Trust Agreement and is to receive income from the Trust to pay his or her living, health care, recreation and other expenses as chosen by the Trustor. Also, the Trustor can reserve the power under the Trust Agreement to direct how the Trustee is to invest and manage the assets of the Trust, and to require the Trustee to pay all or any part of the assets directly to or for the benefit of the Trustor. The Trustor usually reserves the power to terminate or revoke the Trust Agreement and thus regain full ownership of the assets of the Trust.

(2) The Trustor may become "incapacitated", that is, unable to manage his or her affairs without the assistance of another person. In such cases, the Trustee can have sole control of the assets of the Trust, but is required to take care of the needs of the Trustor as the beneficiary of the Trust.

(3) If the Trustee dies, or is not performing properly, the Trustor can appoint a Successor Trustee, or one or more Successor Trustees can already be named in the Trust Agreement.

(4) Under Oregon Statutes, a beneficiary of a Trust (including the Trustor), or the guardian or conservator of such beneficiary, can require an accounting to be prepared by the Trustee and can obtain a court order to enforce this requirement. In the same fashion, a court order can be obtained to appoint a new Trustee or to determine the propriety of the administration of the Trust by a Trustee.

c. What happens when the Trustor is deceased?

(1) When the single Trustor, or the survivor of two Trustors (such as husband and wife), passes away, the Trust assets continue to be managed and ultimately distributed by the Trustee, who is usually a Successor Trustee designated in the trust agreement.

(2) The Trustee pays the expenses of funeral, last illness, income tax and other claims and obligations, using such insurance as is available, then trust assets, and then, if required by the Trust Agreement, distributes the remaining assets to the remaining beneficiaries under the Trust, such as

children, grandchildren, charities and so on. This distribution is similar to what is done under a Will.

(3) Instead of making a distribution soon after the passing away of the Trustor, as discussed above, all or part of the remaining assets may continue to be administered by the Trustee for the benefit of some or all the beneficiaries named in the Trust Agreement. This could be to provide financial assistance to a child, college education for a grandchild, and the like. At a time designated in the Trust Agreement, the assets then remaining in the Trust are distributed to those persons then entitled to receive the same and the Trust is terminated by the trustee.

d. How is the Trustee paid?

(1) Ordinarily, if the Trustor serves as the Trustee, no compensation is paid the Trustee because any such payment would only be ordinary income and taxed to the Trustee.

(2) Banks serving as Trustee have standard fee schedules. These fees are, as a current example from one such bank, 1% annually of the total assets of the Trust and 1-1/2% of the income generated by the Trustee's management of the assets. (For example, a $300,000 in Trust assets would produce an annual fee of $3,000 and if the income generated thereupon was $24,000, then an additional fee of $360 would be earned, for a total of $3,360 for the year involved.) Fees to manage real property vary, depending upon the type of property involved (i.e., bare land versus an apartment house, and so on). An individual person serving as Trustee can have his or her fee set forth in the Trust Agreement, or could be paid on the same basis as if a bank were the Trustee. Banks indicate, however, that they can earn more income for a Trust than the average individual serving as Trustee, who often is not an experienced money manager, but again, an individual trustee can obtain investment advice to help him or her manage the assets wisely.

e. What is a "revocable" living trust?

A "revocable" living trust is one which can be revoked or terminated by the Trustor during the lifetime of the Trustor. Often such Trusts are established by a husband and wife so both of them, or the surviving spouse, has the power to revoke the Trust. Such a revocable Trust becomes "irrevocable" upon the passing away of a single Trustor, and sometimes upon the passing away of either spouse, if husband and wife have been the Trustor. As a matter of common practice, the "revocable" Trust becomes irrevocable when both Trustors, husband and wife, have passed away.

f. What is an "irrevocable" living trust?

An "irrevocable" living trust is one expressed in a signed trust Agreement which cannot be revoked or otherwise terminated, and may not even be subject to amendment. This is unusual since most Trustors want to be able to change their minds and handle their assets in the Trust in different ways from time to time. An irrevocable trust is often part of a plan to save or avoid estate taxes.

g. Can a trust be amended?

Trust Agreements are drafted in many ways but most allow amendment by a single Trustor, or if there are two Trustors, such as husband and wife, then by both Trustors, or the survivor. This is a good feature of the living Trust since circumstances can change and the Trustor might want to provide more or less in the way of support to certain beneficiaries, or exercise the Trustor's powers under the Trust Agreement in a new way.

h. Does a Trustor need a Will?

The Trustor really should have a Will even though the Trustor has signed a Trust Agreement. Such a Will acts to dispose of any assets which might not have been transferred to the Trustee under the Trust Agreement. The Will, however, is usually brief and merely devises (i.e., transfers) the assets of the deceased person to the Trustee of the Trust, making mention of the existence and date of the Trust Agreement. Oregon's law allows such a Will to provide the Trust Agreement may be amended after the death of the Trustor so the assets in the Trust can be managed under an amended Trust Agreement. (Such amendment can be very useful where husband and wife have been the Trustor and the deceased spouse has wanted the survivor to be able to amend the Trust Agreement later to meet changed circumstances.) Often the Will provides if the Trust Agreement has been revoked prior to the death of the Trustor that the assets of the Trustor will be given the certain persons, such as a surviving spouse, children and so on. The Will might also include a "testamentary trust" (discussed below) but this would be unusual since the Trust Agreement is used to express the terms of any trust arrangement and the person signing the Will would rely on the Trust Agreement to carry out his or her wishes. A will that accompanies a trust is often called a “pourover” will.

i. What happens if a Trustor passes away without a Will?

In this case, any assets of the Trustor which have not been transferred during the Trustor's life to the Trustee of the Trust would be distributed pursuant to the law of intestate succession. This is a statute that provides all such assets go to the surviving spouse, if any, of the decedent, if the decedent has had no children or only has had children with the surviving spouse. If the decedent has had children by another spouse, then one-half of the assets go to the surviving spouse to whom the deceased person is married at death and the other one-half goes to the children. If the decedent does not have a surviving spouse, then the assets go in equal shares to the decedent's children (and to any grandchildren who are children of a deceased child of the decedent), and if there are no such children or descendants of such children, then the assets go to other relatives.

4. DISADVANTAGES OF THE LIVING TRUST

a. There is the cost of having the Trust Agreement prepared by an attorney, and a “pourover Will” which refers to the Trust Agreement. Also required are deeds to convey real property, and an assignment or a bill of sale to transfer personal property to the Trustee for administration under the Trust Agreement. There are costs associated with these transfers.

b. There is the work involved in transferring assets to the Trustee, including redesignating the Trustee as owner of bank accounts, certificates of deposit, insurance policies, investment accounts, stocks and bonds and the like. Investment counselors, bank officers, attorneys and other people are available to help accomplish these transfers, however.

c. There is the need for the Trustor to be aware of when he or she is acting as a Trustee, or as a Trustor, or as an individual, in terms of the use and transfer of assets and particularly in regard to signing documents, contracts, checks and other legal instruments. Some people find this bothersome and confusing.

d. There are the Trustee fees to be paid a Trustee if the Trustee is a bank or is a person other than the Trustor who wants a fee to serve.

e. There is no Court supervision for administration where that might be needed, for example, with quarreling beneficiaries, unless a Court action is filed.

f. There is no Court oversight of accountings or other work performed by the Trustee unless a Court action is filed.

g. Probate can cut off creditor's claims against the estate, administration of a living trust ordinarily will not, without a special proceeding being undertaken.

h. Sometimes an individual successor trustee makes mistakes that can be costly to correct.

i. Sometimes an individual successor trustee succumbs to temptation and benefits themselves improperly.

5. ALTERNATIVES TO THE LIVING TRUST

a. During the life of the Trustor

(1) Self-management:

During his or her lifetime, the Trustor can manage his or her own assets. This is what most people do, but Problems can arise due to poor health, mental incapacity and so on, and there is the possibility of some third party trying to take advantage of an elderly or ill person.

(2) Power of Attorney:

Under this device the owner of assets empowers some other person to manage all or part of the owner's assets. This is an arrangement which is easily and inexpensively established by the owner signing an instrument known as a "power of attorney", and the authority of the "attorney in fact" given this power to manage assets can continue even after the mental disability of the owner of the assets. The power of attorney terminates upon the death of the owner of the assets. Special provisions can be included in the power of attorney to require periodic accountings to be furnished to the owner of the assets and the power of attorney can be restricted to only pertain to certain kinds of property, to limit the types of authorized investments and expenditures, and so on.

(3) Conservatorship:

This is a formal proceeding in the local Circuit Court in which a person is appointed by the judge

to be the "conservator" of another person and to manage that person's assets for his or her protection. The conservator is usually bonded and by law is required to file annual accounting with the court. The accountings and other information filed with the court are, however, a matter of public record open to inspection by anyone. There usually are fees, also, to be paid to the conservator.

(4) Guardianship:

Like conservatorship, this is a formal proceeding in the local Circuit Court in which a person called a "guardian" is appointed to take control of the person to be protected. The power of the guardian is over the "person" of the person to be protected, and the guardian makes decisions regarding health care, place of residence and so on which in effect control much of what the protected person is to do. A living trust does not take the place of a guardianship in that the Trustee cannot make this kind of decision concerning the Trustor or any other person who is a beneficiary under the Trust Agreement. Ordinarily the Trust Agreement provides that the Trustee should consult with any guardian, and the work of the Trustee and guardian should be coordinated for the benefit of the protected person. The guardian is authorized by law to receive a fee for services, and must make periodic, written reports to the court which are a matter of public record open to inspection by anyone.

(5) Guardianship and Conservatorship:

This is a combination of the roles of the guardian and conservator in a single court proceeding. One person can be appointed both guardian and conservator for the protection person. Again, however, there are fees to be paid, and the proceeding is a matter of public record.

b. After the passing away of the Trustor.

(1) Personal Representative:

The Personal Representative (also formerly known as the executor, executrix, or administrator) is the person charged with the legal responsibility to administer the estate of a deceased person. The Personal Representative may be an individual or a bank authorized to do such work. The judge of the Circuit Court, once a probate proceeding is filed, appoints the Personal Representative, who is customarily bonded and then has the responsibility to pay funeral bills and other obligations of the decedent and ultimately to distribute the assets of the decedent to those entitled to receive the same under the Will of the decedent, or if there is no valid Will, then pursuant to the law of intestate succession which has been referred to above. If the decedent has a Will which includes a testamentary trust, referred to below, then the Personal Representative distributes the remaining assets to the Trustee of the testamentary Trust.

(2) Testamentary Trust:

A Trust may be established pursuant to the Last Will and Testament of the decedent. This is known as a "testamentary trust" because it is created pursuant to a Will. A Trustee is named in the Will and may be an individual person or a bank authorized to exercise the powers of a Trustee. The Trustee receives the assets subject to administration under the testamentary trust from the Personal

Representative of the deceased person's estate upon the completion of the probate proceeding. A testamentary trust can provide for various beneficiaries, of course, such as a surviving spouse, children, charities and the like, and after the passage of time, as provided in the testamentary trust, then the remaining assets are distributed to beneficiaries as provided in the testamentary trust by name or through some other means of designation.

(3) Small Estates:

Small estates are those in which a deceased person passes away owning not more than $75,000 in value of personal property (i.e., cash, investment accounts, furniture and so on) and $200,000 in value of real property (i.e., a home). Oregon's law provides for the filing of an affidavit in lieu of a formal probate proceeding, and no Personal Representative is appointed for the administration of the estate.

6. ESTATE AND INHERITANCE TAXES

A trust does <u>not</u>, without special provisions, reduce or eliminate estate or inheritance taxes.

The federal estate tax is imposed on estates exceeding $5,250,000.

Each individual has a $5,250,000. federal estate tax exemption. There is also an unlimited marital deduction for transfers between spouses during life and at death. <u>With proper planning these concepts allow a couple to pass $10,500,000. to children or others federal estate tax free.</u>

This kind of tax planning is possible with living trusts or with wills. Special language is necessary in the applicable documents and other actions are necessary to accomplish these purposes.

The laws pertaining to estate tax change often. Please be sure to seek specific advice for your situation and do not rely on this general information.

Please note the Oregon estate tax exemption is only $1,000,000 and so some estates may be subject to Oregon inheritance tax but not federal estate tax. The Oregon exemption has remained unchanged since Oregon "uncoupled" from the federal exemption.

This information is general in nature and not specific advice for you or your situation.

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