

TRUSTS: Part 1
BASIC PRINCIPLES

by
PI-YI MAYO*
ATTORNEY AT LAW
*Of Counsel to the
Randy Drewett Law Firm

TRUSTS: Pt. 1 - Basic Principles

I. WHAT IS A TRUST?

When you were a child, did you ever give a trusted possession such as a baseball or a secret decoder ring to a good friend and tell him or her to hold it for you and if you never made it back from summer camp to give it to another one of your best friends? If you did, then you created a trust. Most trusts we hear about are trusts that hold large sums of money or property for the benefit of a charity or some heir to a family fortune, but a trust can be a very simple thing.

In the example above, the person creating the trust is known as Grantor or Settlor. The friend who holds the property is known as the Trustee. The orders that you gave your friend (the Trustee) about what to do with the property (sometimes called the Corpus) would be the terms of the trust. The remaining player in the transaction was your friend whom you wanted to have the decoder ring and he or she is called the Beneficiary. In this case, as is often the case, the Beneficiary may have never even known of the existence of the trust until and if the property was delivered.

II. REVOCABLE AND IRREVOCABLE TRUSTS.

If, when you delivered the baseball to your friend (Trustee), you told him or her that if you made it back from summer camp, and didn't get eaten by Bigfoot, and you want your baseball back, you have created a revocable trust. If, on the other hand, you really wanted your other friend (the Beneficiary) to have that baseball but you know that in a weak moment you might change your mind and try to get it back, then you might tell your friend (Trustee) that he should never give the baseball back to you. He was to hold it until some other event happened, such as your moving away and never returning to your current home. At that point, you would have created an irrevocable trust. In one case, you can change your mind and revoke the trust and everything goes back to the way it was before you created the trust, and in the other case, once the trust is created, you cannot undo it.

III. INTER VIVOS AND TESTAMENTARY TRUSTS.

The trust you created above was called an inter vivos trust. It was created during the lifetime of the Grantor (you). Depending upon whether you wanted to get your baseball back, the inter vivos trust could be a revocable trust. If you wanted to save yourself from that moment of weakness, it could be an irrevocable inter vivos trust, meaning you created it in your lifetime and wanted to make sure you could not change your mind and get it back.

Many times people want to create trusts but they don't want to part with the baseball just yet (in case a hot game breaks out) but they would like to have the trust take effect after their death. They create a trust, put all the instructions and name a Trustee and the Beneficiary in their will. This type of trust is called a testamentary trust. The will does not take effect until after the person has died so the trust is not created during the lifetime of the Grantor.

IV. LIVING TRUSTS

There is a lot of information available today about something called a "living trust". A living trust is a trust that is created during the lifetime of the Grantor or Trustor so it is an inter vivos trust. Most of the time, it is a revocable trust meaning that the Grantor or Trustor can change their mind and revoke the trust at anytime. The principal purpose is to pass the property to someone after the death of the Grantor without the requirement of probate proceedings. Another purpose can be to provide for the management of the assets of a person if that individual were to become unable to handle their own affairs at some point in their life.

Most of the living trusts are revocable trusts and most often they name the Grantor or Settler the Trustee of the trust so that the creator of the trust or the owner of the assets placed in the trust can continue to manage the assets placed in the trust once the trust is in effect. The trust may contain provisions that allow another person to take over as Trustee (usually called an Alternate or Substitute Trustee) if the person who created the trust becomes unable to take care of their affairs. It is important to note that in some states the probate process is a difficult and expensive undertaking. This is not the case in Texas. Our probate code allows for very quick and inexpensive administration of estates and although the use of living trusts to avoid probate is standard practice in other states, avoidance of probate by the use of a living trust in Texas may entail greater expense and difficulty than the probating of a will.

The marketing of living trusts has been the subject of some controversy in our State in recent years. Many times nonlawyers attempting to sell financial products or services will use the issue of avoiding probate with the use of a living trust as a marketing ploy to get people interested in their lectures or seminars. No one should decide to purchase or create such a trust without the advice of a competent, trusted attorney. The creation and administration of a living trust is a very serious legal step and it should only be taken with the advice of legal counsel.

V. MILLER TRUSTS

Most Texans who spend more than a very short time in a nursing home will need to qualify for Medicaid to obtain help in paying for the care they receive. In Texas, the Medicaid program has an "income cap". If your income from Social Security or a pension exceeds \$1536.00 a month, then you do not qualify for Medicaid. This limit on income eligibility exists only in a few states in the country. This income cap resulted in some people not being able to qualify for benefits in Texas when a person with the same income living in many other states would have been able to qualify. This situation was just not fair. Congress recognized the inequity the law created and passed a law that allowed the creation of something called a Miller Trust. In the states that have an income cap, this trust allows for income and only income to be placed in a trust and once they are placed in the trust, this income no longer counts against the "income cap". The important thing to understand about a Miller Trust is that it is not a vehicle or device to hold any assets. It receives only income. Stocks or bonds or CD's cannot be put in a Miller Trust. Once the income is placed in the trust, the person will be treated for eligibility purposes the same as any person with income below the cap. For all intents and purposes, the Miller Trust eliminates the income cap as a bar to eligibility for persons seeking Medicaid for long term care in Texas.

VI. CONCLUSION

Trusts can be a very important tool for many people to use in their estate plans to achieve many different results. They can be used to plan for the disposition of assets after the death of the owner or they can be used to help manage the assets of a person during their lifetime. Trusts can be as simple or complex as the purposes for which they created. Trusts can be used to avoid probate or to protect a spendthrift from losing an inheritance. The most widespread use of trusts today would be in the area of estate tax planning. The trusts created for this purpose can be and most often are very complex. No matter what the type of trust or the reason for which it is created, the most important thing to remember is to obtain the advice of competent legal counsel when dealing with this area of law. The law of trusts can be very complicated and assistance of a lawyer experienced in trust law is paramount when deciding whether a trust is the proper legal device to help anyone obtain their goals.