

# Promissory Notes and Revocable Trusts

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You may know that with a Revocable Trust, you should take steps to transfer your assets into your trust during your lifetime, to ensure it accomplishes your goals (such as probate avoidance, estate tax reduction, and providing for your beneficiaries). This particularly is important when you have a promissory note.

## Promissory Notes

A promissory note is a written promise by one party (the “maker”) to pay a sum of money to another party (the “payee”).

A promissory note, if assignable, can be transferred to your Revocable Trust by assigning

the beneficial interest in the note to your Revocable Trust. If the note is secured, the security

should also be assigned. This assignment is accomplished by the payee signing over the note to the trustee or trustees of the Revocable Trust. The assignment should be in writing and a copy of the promissory note should be attached.

Once a promissory note has been assigned to a Revocable Trust, the payee should notify the maker and instruct them to remit future payments on the note to the trustee rather than the original payee.

Why is this so important?

Here's an example:

John and Jane have a joint revocable trust that provides for each other and upon their deaths, the trust is to be divided among their four children. One child, Amy, borrows \$300,000 from her parents to purchase a home. She signs a promissory note and a mortgage is recorded. The note is payable back to John and Jane. John and Jane don't tell their estate planning attorney about this transaction. Often clients don't consider the outstanding notes that they have between themselves and their adult children.

When you loan money to your children, it's always a good idea to inform your estate planning attorney about these agreements to ensure that your intent is properly followed through. Another issue that arises is when the note is never repaid, including interest on the loan. When this occurs, the IRS requires individuals to impute an interest rate if one isn't stated resulting in taxes.

Another issue that can occur is that upon the deaths of the parents, if the note hasn't been paid in full, the note will be a probate asset and the mortgage cannot be discharged unless a probate is filed-a process that can add delay and cost.

Perhaps, many years later when both Ken and Barb are deceased and their estate is being administered, their children will find out about the note, as Amy was the only person who knew about it. What if none of the note had been repaid? What was the intent of their parents? Does Amy still owe the outstanding note to her siblings?

Make sure that your estate plan considers all of the issues and context associated with lending money to children or other relatives. Otherwise, your children may have to sort through these problems, which can cause conflict among them.

*The information contained in this article is not intended to make you an expert on estate planning nor is this article intended to replace the need for the advice of a professional. Rather, this article is simply intended to provide a basic understanding of why estate planning is important for everybody and a basic understanding of some of the more common estate planning tools. This article does not constitute legal advice.*