The Number One Reason Why Trusts Fail

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A trust can have powerful benefits – avoiding probate and saving legal costs, reducing estate taxes, protecting assets from long term care costs, addressing unexpected events, preserving benefits for the disabled, and the list goes on. (To learn more about trusts, you can read my blog about them here.)

But many trusts fail to work as intended.

I know because I see failed trusts all the time. In my experience, there is one primary reason why a trust fails: it wasn't properly "funded."

What does it mean to "fund" my trust? Funding your trust is the process of transferring your assets from you to your trust. To do this, you physically change the titles of your assets from your individual name to the name of your trust. Think of the trust like a basket. In order for the instructions you set up in your trust to work as intended, there need to be assets in the "basket."

It seems like a simple concept, but I am often amazed at how many clients come to me with unfunded trusts from other firms (which leaves me to wonder whether the importance may not have been emphasized enough).

Let me give a simple example. Suppose Joe wants to avoid probate. He owns a checking account, a brokerage account, a house, and a vacation home in another state. His son, who would be the Personal Representative if Joe had a probate estate, lives in California.

Joe wants to avoid probate for various reasons, including avoiding an ancillary probate proceeding for his out-of-state property, saving his son the inconvenience of having to travel to deal with probate proceedings, and reducing legal fees for his estate.

Joe decides to create a revocable living trust that will own his assets while he is alive. Joe will be the trustee. When he dies, his son will become the trustee and will pay Joe’s debts and taxes before distributing the assets to Joe’s loved ones. Good plan – if done properly, Joe’s estate will avoid probate. His son can probably manage the estate without setting foot in a probate court room.

To make his plan work, Joe needs to do two things: (1) create a revocable trust, and (2) fund the trust.

Joe goes to a lawyer to have his revocable trust drawn up.

Now comes the crucial next step: funding the trust. Joe needs to go to his bank to have the checking account changed so that the bank records show the trust (not Joe) as the owner. He needs to sign new deeds that transfer ownership of his house and vacation home from Joe to the trust. He also needs to re-title ownership of the stock into the name of the trust.

If Joe does those things, his trust should work as intended.

Now imagine, when Joe dies, his son discovers that significant assets are still titled in his father’s name, not in the name of the trust. So, now we will need to administer the trust, and file a probate with the court. Unfortunately, situations like this occur all the time.

Seek advice and guidance from a qualified estate planning attorney who is committed to making all trust clients aware of the importance of trust funding and working with them to ensure each trust prepared is properly funded.

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.