CHAPTER 50

Revocable Living Trusts – Separate or Joint

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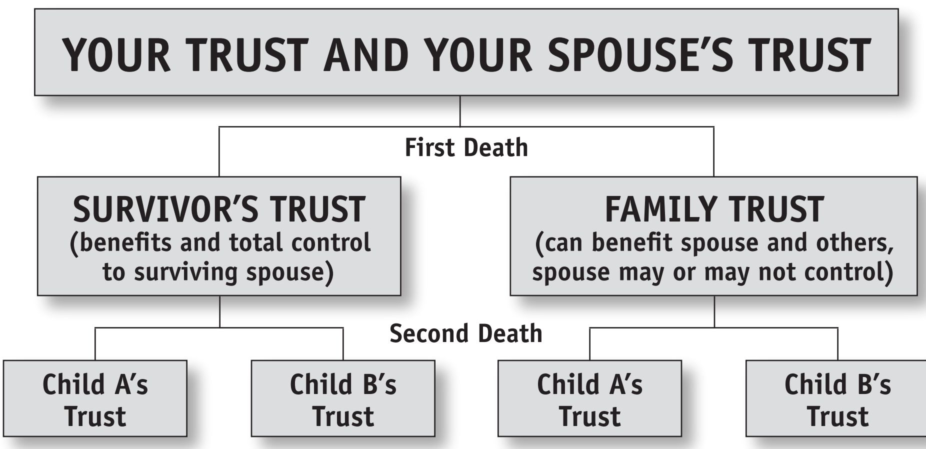
You have decided on a revocable living trust because you like the speed, convenience, and privacy a trust offers. Now, should you and your spouse put all of your assets into one trust or should each of you have your own? Picking the right type of trust can make life easier for you and for those who have to manage your trust when you cannot do so yourself.

If your estate is larger than the federal estate tax credit ($2 million in 2008 and $3.5 million in 2009), part of your revocable trust will include tax planning. Tax planning can mean the creation of a new trust after your death for your spouse's benefit (or after your spouse's death for your benefit). The new trust takes advantage of the estate tax credit and various planning options. A typical joint revocable trust for an estate worth more than the estate tax credit works like this:



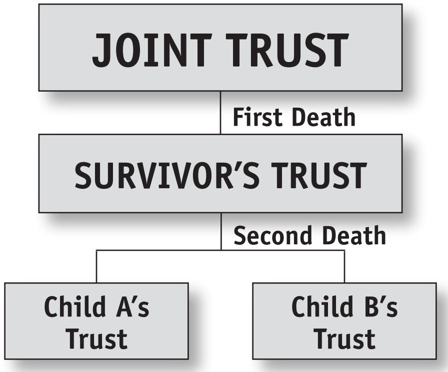
Trusts for the benefit of the same person can usually be consolidated, but your trust is still rather complicated with lots of sub-trusts. The more complicated a trust, the more difficult it will be for your successor trustee to take over. The more trusts you put in one document, the bigger the document and the more cumbersome it is.

If you chose a trust for its privacy, having more trusts inside your trust could jeopardize that privacy. Often copies are required of various trusts — a special needs trust will need to be sent to the state for approval and some banks require a copy of the entire trust before accepting an account. If you have everything in one trust and a copy is required of a particular part, you may need to provide the entire document and your privacy will be lost.

If you are in a second (or subsequent) marriage, you may want separate trusts. A separate trust contains only your assets. Your spouse can have a separate trust with only his or her assets. You can choose to support your surviving spouse, and even allow your spouse to be trustee, while still insuring your family benefits. Stepchildren worry that the stepparent will disinherit them, which can be a viable concern. A separate trust insures your children know that although you are providing for your surviving spouse, they will still get their great-grandmother's piano and their grandfather's Exxon stock. Having stepchildren act as trustees for a surviving spouse is generally not a good idea. Every dollar spent on your surviving spouse is a dollar your children do not get, which is a classic conflict of interest. To reduce potential sources of conflict, using a corporate trustee or an impartial friend may be your best option.

If you brought assets to your marriage, a separate trust is a good option. Perhaps you inherited the money, or it came from a prior marriage, or you married after you had already created wealth. A separate trust requires that the assets be kept separate. If you do not keep an asset separate, by putting the asset into a joint bank account, for example, and barring a written agreement to the contrary, you have given half of it to your spouse (laws differ by state, however, and you should consult with an attorney in your state). Although you can argue later that it was not a gift — a difficult argument to prove — separating the assets later is no easy task.

Even with an estate totaling less than the amount of the federal estate tax credit, revocable trusts are wonderful for the simplicity, beneficiary protection, and control they provide. If your estate is less than the federal estate tax credit, you do not expect much asset growth, you and your spouse own everything jointly, and — most importantly — you want the same people to get all of your assets, then you have a perfect situation for a joint trust. In a joint trust, both you and your spouse place all of your assets in the same trust. You and your spouse may be the initial trustees and both of you can make changes. A typical joint trust structure for an estate totaling less than the federal estate tax credit looks like this:



A joint trust is also a great idea in Community Property states: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin. Community Property law (in general) provides that all assets acquired during marriage from the work of either spouse are owned half by each spouse. A joint trust preserves the status of the Community Property and its considerable estate tax advantages.

The estate tax advantages include a double-step up in basis of the Community Property at the death of the first spouse. Basis is your investment in an asset. If you buy stock for $1, your basis is $1. If you later sell it for $10, you have a gain of $9 (Sale price minus basis). You pay capital gains tax on gains. The greater the basis, the less your gain and the less capital gains tax you pay.

In Common Law jurisdictions (non-Community Property States), any property that you own jointly with your spouse is considered half yours. Only half is included in your estate and only half receives a step up in basis. If you own that same $1 stock jointly with your spouse and it is worth $10 when you die, the basis in the stock increases from $1 to $6. The basis in your half ($1) stepped-up to the date of death value ($5) plus your spouse's basis ($1). In Community Property jurisdictions, both your half and your spouse's half receive a step up in basis. So at your death, you and your spouse have a total basis in the stock of $10. If you sell the stock in a Common Law jurisdiction, you will pay tax on $4 ($10 - $6). If you sell the stock in a Community Property jurisdiction, you own no capital gains tax ($10 - $10).

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