ONE SOLUTION FOR unmarried couples who own real estate together is to use a joint revocable trust, similar to the joint trust used by married couples in community property jurisdictions as their primary estate planning document. The trust usually provides that while both spouses are alive they are both beneficiaries of the trust and both hold powers of revocation and amendment. At the death of the first spouse, the trust assets are divided into the deceased spouse’s assets and the survivor’s assets, and the deceased spouse’s assets are held in further trust or distributed in a manner consistent with the deceased spouse’s intentions (including tax planning). At the death of the survivor, the trust agreement generally provides for distribution of the survivor’s assets (including holding in further trust) in a manner consistent with the survivor’s intentions. The joint trust is the primary estate planning document for the couple, and each spouse executes a pourover will that names the joint trust as the beneficiary of the estate.

Joint trusts have not been traditionally used in common law states for married couples. More common is the practice of creating a separate trust for each spouse. The uncertainty of gift tax consequences and the possibil-
ity of adverse estate tax consequences caused practitioners to favor separate trusts. In community property states, however, joint trusts are favored because the spouses own undivided interests in the community property. The increase in the exemption from federal estate tax, and the wave of state legislation allowing tenancy by the entireties property (which has favorable creditor protection but is only available to married couples) to be placed into trust have made joint trusts more attractive in common law states. These materials address the advantages and disadvantages of joint trusts for co-ownership of real estate by unmarried couples.

I. Reasons for Using the Joint Trust

A. Simplification and Maintenance of Joint Ownership. With a joint trust, property held jointly by the couple does not need to be split between two trusts. The couple’s perception of joint ownership is retained. The joint trust also simplifies the estate plan where the couple have a unified intention to benefit the survivor and the couple’s descendants.

B. Management. If both members of the couple are co-trustees, then they each hold management power over the property in the trust. If one becomes incapacitated, the other can manage the property without invoking a power of attorney or establishing a guardianship. When both are acting as co-trustees, both will most likely need to join in transactions unless altered in the trust agreement, and depending on governing state law.

C. Efficient Transfer at Death of First. The trust instrument can provide for disposition of the property at the deaths of the co-owner. At the death of the first partner, the trust can continue for the lifetime of the survivor, although the trust will no longer be revocable as to the first to die’s interest in the property.

II. Drafting the Joint Revocable Trust

A. Power to Amend or Revoke While Both Partners Living. Clients may prefer that any amendments or revocation require the joint action of both owners, but that restriction may create gift tax issues. Although a trust funded with only co-owned property would not trigger a gift to either partner, arguably the partner with shorter life expectancy may be considered to be making a gift to the younger partner. Treas. Reg. § 25.2511-2(b) states that a gift is complete if the donor has no power to change disposition of the property; and Reg. § 25.2522-2(e) provides that the donor is not considered to have retained the right to revoke if that right is exercisable jointly with a person who has a substantial adverse interest.

The Uniform Trust Code addresses the ability to revoke or amend a revocable living trust where there is more than one trustee:
If a revocable trust is created or funded by more than one settlor: (i) to the extent the trust consists of community property, the trust may be revoked by either spouse acting alone but may be amended only by joint action of both spouses; (ii) to the extent the trust consists of property other than community property, each settlor may revoke or amend the trust with regard the portion of the trust property attributable to that settlor’s contribution; and (iii) upon the revocation or amendment of the trust by fewer than all of the settlors, the trustee shall promptly notify the other settlors of the revocation or amendment.

UTC § 602(b). Regardless of whether this provision has been adopted in the state, the trust agreement should contain a comparable provision specifying that either partner/trustor can amend or revoke with respect to his or her interest in the trust.

In addition, PLR 200101021 (10/2/2000) illustrates another satisfactory approach. The trust in that ruling was a joint spousal trust, funded by tenancy by the entirety property owned by the grantors. Either grantor had the right to amend the trust, and either grantor had the power to terminate. Upon termination, the trust property was to be delivered to the grantors as tenants in common. The IRS concluded that the each grantor’s power to terminate and receive his or her property back meant it was not a completed gift. Reg. § 25.2511-2. Note, however, that in this case each grantor made an equal transfer of property. If one partner transfers a larger amount of property to the trust, then each partner must receive what they put in at termination in order to fit within the letter ruling. If the clients prefer that the property be distributed equally on termination even if not equally contributed, there will be a completed gift. Therefore, the trust should provide that each partner has the unilateral right to terminate the trust, and the distribution of the property upon termination should be spelled out in the agreement. See PLR 200210051; PLR 200403094.

B. Funding on the Death of the First Partner.

1. Avoiding Completed Gifts.

The trust agreement must make clear that the survivor retains the right to revoke and amend the survivor’s trust, in order to avoid a completed gift to the remainder beneficiaries of the survivor’s share. In addition, there should be a direction that all taxes and expenses chargeable against the decedent’s estate and debts of the decedent must be paid from the decedent’s share to avoid a gift by the survivor to the remainder beneficiaries of the deceased trustor’s share.

In addition, the survivor’s ability to revoke or amend the survivor’s portion of the trust even if incapacitated should be protected. For example, the trust can provide that if the survivor is incapacitated, an attorney-in-fact for the trustor can exercise those powers. The UTC allows attorneys-in-fact to exercise revocation and amendment powers only if the trust agreement or power of attorney so provides, so specific language authorizing an attorney-in-fact should be included in the agreement.
2. How Not to Draft a Joint Trust. In *Ike v. Doolittle*, 61 Cal. App. 4th 51, 70 Cal. Rptr.2d 887 (1998), the joint revocable trust at issue had an impressive number of drafting errors. First, the wife had significant separate assets, and the trust specified that the separate and community assets of the spouses retain their character, but the spouses also signed an agreement the same day purporting to convert all of their property to community property. Next, the trust was to be divided on the death of the first spouse into Trust A (the survivor’s trust) and Trust B (up to the unified credit amount available to the decedent). However, the revocation and amendment provision stated that after the death of the first Trustor, the survivor would have the power to revoke or amend “the Trust” rather than limiting the survivor’s right to revoke or amend to the survivor’s share of the trust. This threatened to include Trust B in the survivor’s estate.

An additional error was a provision directing that Trust B (the credit shelter portion from decedent) be merged into Trust A (the survivor’s trust) upon the death of the survivor: “upon the death of the Surviving Trustor, Trust ‘B’ shall terminate and the undistributed net income and principal of Trust ‘B’ shall be merged with the undistributed net income and principal of Trust ‘A’…” Trust B was already includable in the Survivor’s estate because of the faulty revocation clause, but the merger clause presented an additional reason for inclusion in the survivor’s estate, since the survivor controlled the remaindermen of Trust A even if the revocation clause did not apply to Trust B.

The most problematic drafting error was in the provisions providing for distribution on the deaths of both Trustors. Mr. Ike and Mrs. Ike had different remainder beneficiaries that they intended to benefit. Mr. Ike had sons from a prior marriage whom he named as remainder beneficiaries and Mrs. Ike had 11 designated beneficiaries, including a nephew. She excluded several other family members who would be her intestate heirs. In the section directing distribution on the death of the surviving trustor, the agreement stated “If [Mr. Ike] is the Surviving Trustor,” his separate property and his one-half interest in the community shall be distributed to his sons, and it provided that if Mrs. Ike was the survivor, her separate property and her one-half of the community would be distributed to her 11 beneficiaries. This provision presented several problems. First, the trustors’ intention was that upon the death of the survivor, whoever that may be, Mr. Ike’s share of the property be distributed to his sons, and Mrs. Ike’s share be distributed to her named beneficiaries. Mr. Ike was the surviving trustor, so his sons were entitled to his share of the assets, but the trust agreement did not say who was to receive Mrs. Ike’s share of the assets. Also, at Mrs. Ike’s death, i.e., the first to die, the assets had been divided as follows: $600,000, which constituted all of her separate property and a portion of community sufficient to equal $600,000, was placed into Trust B, the credit shelter trust. The remainder of the community property and Mr. Ike’s separate property (which was nominal) went into Trust A. It is unclear whether any of the community that went into Trust A had been part of Mrs. Ike’s share. However, the distribution language did not take into account that the property would no longer be identifiable as separate or community as of the survivor’s death.

And there was another problem: the trust agreement also contained a clause that gave any portion of the trust not disposed of to the “legal heirs of each Trustor.” It apparently did not specify how that would be divided between the two sides of the family. Based on this clause, the intestate heirs of Mrs. Ike had made
claims to the assets. Fortunately, California law gave the court sufficient authority to reform the trust instrument to carry out the trustors’ actual intent.

III. Funding with Residential Real Property

If a client chooses a revocable living trust as the primary estate planning document, transfer of the home into the trust is necessary to avoid probate. One early concern was whether such a transfer would trigger a due on sale clause in any mortgage or deed of trust secured by the property. The Garn-St. Germain Depository Institutions Act, however, now prohibits the triggering of a due on sale clause for a transfer of most residential property “into an intervivos trust in which the borrower is an remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property.…” 12 U.S.C. § 1701j-3(d)(7).

The trustor will also want to add the trust to the homeowner’s insurance policy and to the title insurance policy. The title insurance policy may address such a transfer or may require a separate endorsement and small fee. The trustor should also check with the title company regarding the form of the deed; some companies will only continue insurance if a warranty deed is used.

In the states that have addressed the issue, homestead protection will be continued if a residence is transferred into a revocable trust. In Fitton v. Bank of Little Rock, 365 S.W.2d 888 (Ark. 2010), the Arkansas Supreme Court held that transfer of a homestead into the resident’s revocable living trust does not remove homestead protection. In that case, the husband and wife had each transferred their one-half interest in the residence into their respective revocable trusts. They separated, and the husband immediately mortgaged his one-half interest, waiving his homestead exemption. The husband’s one-half of the residence was awarded to the wife in the divorce proceedings, but there was nothing requiring her to assume liability for the mortgage taken by the husband after separation. She transferred the husband’s one-half into her trust. She did not pay the mortgage, the bank foreclosed, and she argued that she never waived her homestead rights and so the debt was not collectible. The bank argued that a trust owner could not assert homestead, but the Arkansas Supreme Court disagreed and held for the wife. The Fitton court relied on a Kansas case with a similar holding, Redmond v. Kester, 159 P.3d 1004 (Kan. 2007). New Hampshire clarifies the issue by statute. Gen. Stat. § 480.9 states:

A conveyance of real property by deed to one or more trustees of a revocable trust shall not result in the loss of homestead rights of any person executing the deed (unless the deed contains an express release of homestead rights by such person) provided that such retained homestead rights in any such property shall not be enforceable against any other person to the extent such other person acquired an interest in or lien on the property after its conveyance into the trust without having notice of the revocability of the trust. Such notice may be given by the inclusion of the word “revocable” in the name of the trust as recited in the deed, or by the recitation in the deed or a subsequently recorded document that at the time of the conveyance the trust was a revocable trust.

In a 2001 federal bankruptcy case, In re Bosonetto, 271 B.R. 403 (Bankr. M.C. Fla. 2001), the federal bankruptcy court held that Florida’s homestead exemption did not apply to a residence held in the bankrupt’s

If your client is concerned about creditor issues, the available authority would support the homestead. However, you should either warn the client of the risk or, if the client wants to be conservative, delay making the transfer. One possible solution to this would be the transfer on death deed. There is a uniform law, adopted in 8 states and being considered by several others, called the Real Property Transfer on Death Act, that would allow a transfer on death designation in a deed similar to a payable on death beneficiary designation on a bank account. One popular use of this device is to name the property owner’s revocable living trust as the death beneficiary. The residence could therefore stay out of the trust for the trustor’s lifetime, making it easier to sell and mortgage the property, and the residence would by virtue of the transfer on death deed be distributed to the trust without the need for probate.

If the client has residential property in another state that needs to be transferred into the revocable trust, you should first check to see if the transfer on death deed is authorized in that state. Next, you need to consider whether you are authorized to prepare the deed to transfer the property. Generally, preparation of a deed for real property is the practice of law in the jurisdiction where the property is located, and unless you are licensed in that state, you would be engaging in the unauthorized practice of law to prepare the deed. However, many states have exceptions to their ethics rules that allow limited practice. The ABA model Rules of Professional Conduct 5.5(c)(4) allow a lawyer admitted in another U.S. jurisdiction to provide legal services on a temporary basis in the jurisdiction adopting the rule under several different circumstances, including services that “arise out of or are reasonably related to the lawyer’s practice in a jurisdiction in which the lawyer is admitted to practice.” The California rule is found in a court rule, Rule 9.48. You therefore need to research whether the state in which the property is located allows you to provide temporary legal services, and if not, hire counsel in that state to prepare the deed.

Final regulations under IRC § 121 specify that a taxpayer can claim the exclusion of gain on sale of a residence held in trust if the taxpayer is treated as the owner of the trust under grantor trust rules. Reg. § 1.121-1(c)(3). Since a revocable trust is a grantor trust, exclusion of gain on sale is available.

IV. Administration Issues After One Spouse Dies.

A. Amendments to Survivor’s Trust. Frequently, upon the death of the first trustor, the survivor chooses to amend his or her portion of the trust. In some cases, it may be as a result of the survivor’s decision to treat the children differently than the original plan contemplated. If the survivor remarries, it is likely the survivor will want to make provision for the new spouse. Having the assets in the revocable trusts helps in the remarriage setting to keep the assets segregated, but the amendments to the original joint trust can become cumbersome.
The case of *Manary v. Anderson*, 176 Wn.2d 342, 292 P.3d 96 (2013), illustrates the problems that can be encountered if a revocable trust is not properly administered after the death of the first spouse. Mr. and Mrs. Greene established a joint revocable trust and transferred their community property residence into the trust. The trust provided that upon the death of the first spouse, the trust estate would be divided, the deceased spouse’s share would be placed in the “Family Trust,” which would be irrevocable, and the survivor’s one-half would be placed in the revocable Survivor’s Trust. Mrs. Greene died, but Mr. Greene as successor sole trustee did not create the two separate trust shares. He amended the trust to replace the original remaindermen with his sister. A longtime family friend, Mr. Anderson, then became Mr. Greene’s “companion and caretaker,” and Mr. Greene executed a Will leaving the residence to Mr. Anderson. He did not refer to the trust in his Will or acknowledge that the residence was held in the trust. After Mr. Greene died, Mr. Anderson was appointed executor of the estate and he took possession of the residence. Mr. Greene’s sister sued Mr. Anderson, claiming she was entitled to the residence as remainder beneficiary of the trust. The gift in the Will would not be recognized as a valid trust amendment but Mr. Anderson claimed that the gift in the Will was valid under the Washington Superwill statute. That statute, RCW 11.11, allows a testator to change the beneficiary of certain types of nonprobate assets in a later-executed Will. The Washington supreme court held that Mr. Greene’s interest in the trust was a nonprobate asset within the meaning of the Superwill statute, and that he had met the requirements of the statute, so Mr. Anderson was entitled to Mr. Greene’s interest in the residence. The court did not directly address who was entitled to Mrs. Greene’s one-half interest in the residence but implied that the decision applied only to Mr. Greene’s interest. Apparently the original remaindermen, who would be entitled to the one-half portion directed to be placed in the irrevocable portion upon the first spouse’s death, were not party to this lawsuit, although the caption identified “unknown John Does 1-5” as additional defendants.

**Bibliography**

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California Legal Forms: Transaction Guide ch. 70 (includes forms; available on LEXIS)


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