Using a trust as part of your estate planning strategy

A trust is a legal arrangement established by the owner of assets (grantor) in which a person(s) and/or entity (trustee) holds title to assets that are managed on behalf of others (trust beneficiaries). Trusts can play a useful role within estate planning strategies.

Familiarizing yourself with the basic types of trusts and how they are utilized can prepare you for conversations with your financial professional about trust strategies and options.

Below are some things you should know about trusts and their role in estate planning.

There isn't just one type of trust.

There are two main types of trusts: revocable and irrevocable.

Revocable trusts, established during life, are also known as living trusts. With them, you can:

- Make changes at any time
- Maintain control of the assets during your lifetime
- Handle your affairs if you're incapacitated
- Help your estate avoid probate

There are multiple types of **irrevocable trusts**, established during life, depending on your end goals, but generally, an irrevocable trust helps:

- Reduce estate taxes
- Protect yourself and the trust beneficiaries from creditors
- Handle your affairs if you're incapacitated
- Your estate avoid probate

Trusts do have drawbacks.

Whether you choose a revocable or irrevocable trust, there are limitations you'll need to consider. With a revocable trust, you won't receive any tax benefits because the assets are still considered owned by the grantor. Creditors are also still able to make claims against a revocable trust.

With an irrevocable trust, you give up ownership of those assets to an appointed trustee. Any changes may require the approval of all of the beneficiaries and/or a court. Additionally, irrevocable trusts are complicated legal documents that may require outside expertise from an attorney.

A credit shelter trust is a common type of irrevocable trust in estate planning.

A credit shelter trust (also known as a bypass trust or an A/B trust) helps married couples reduce or avoid estate taxes. Generally, it's created after the death of the first spouse and held apart from the estate of the surviving spouse. This helps pass the trust assets estate tax-free to the remaining heirs/trust beneficiaries after the death of the second spouse.

Many assets can be used to fund trusts.

Nearly any type of asset can be used to fund a trust, including stocks, bonds, cash, mutual funds, real estate property, life insurance and annuities, unless restricted under state trust law or the trust document. Life insurance and annuities are becoming common ways to fund a trust.

There are different reasons to choose an annuity or life insurance inside a trust.

You can consider using an annuity if the income beneficiary (often the surviving spouse) is uninsurable or the premium isn't economical.

A life insurance death benefit is generally paid to any beneficiary income tax free, and the gain in a nonqualified annuity is taxable when paid to the beneficiary. Also, it is possible for the beneficiary to receive more death benefit from life insurance than a nonqualified annuity if the grantor dies in a shorter period after establishing the contract.

Life — Life insurance can provide a benefit when owned by a trust. Not only does the trust not have to recognize income from any gains in cash value of the life insurance policy, the death benefit generated by the product can also be income and estate tax free.

Annuity — Annuities can provide an effective way to manage trust assets and pass them on to the trust beneficiaries. Trusts are able to own annuities and receive tax deferral on any gains as long as the trust is acting as an agent of a natural person.

Once assets are transferred to an irrevocable trust, they generally cannot go back to the grantor, and it may not be possible to change the terms of the trust. If you are uncomfortable giving someone else irrevocable control over your money, a revocable trust might be more in line with your goals.

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