Using a Testamentary Trust to Simplify Probate:
A Strategy for the Client without a Revocable Trust

By Walton Davis

A few years ago, I helped an executor administer an estate that poured over to an unfunded revocable trust. Although the decedent failed to use the trust to avoid probate, the trust made probate easy. The executor immediately transferred all the probate assets to herself as trustee and conducted the administration privately inside the trust. The probate proceeding was like a surviving spouse's summary administration: there was only one beneficiary, the trustee, who received all the assets soon after the decedent's death subject to the estate's liabilities.

After filing the inventory, her accounting to the probate court was brief. She reported one receipt, a refund collected after the inventory was filed, and no disbursements because the trustee, not the executor, paid the estate liabilities. She reported distribution of all assets to herself as trustee, the sole beneficiary under the will.

She still had to administer the trust. She paid the liabilities of the estate and trust, accounted privately to the true beneficiaries and distributed the net assets to them. Because of the abbreviated probate, though, she and I did not work as hard as we would have without the trust.

This easy probate is also available to folks who do not need or want a revocable trust or cannot afford one. A stand-alone will can leave everything to a testamentary trust, appoint the same person as executor and trustee, and require the trustee to pay all estate liabilities. Upon the testator's death, the executor can immediately distribute everything to himself as trustee and administer the estate inside the trust. The true beneficiaries are named in the testamentary trust. The trust terminates after all estate liabilities are satisfied. Under N.C.G.S. Section 36C-2-209, the administration of this trust is private unless the will requires the trustee to file court accountings.

A brief accounting is not the only advantage. The accounting is easy to prove to the court. The executor makes no disbursements and so is relieved of delivering the stack of canceled checks and bank statements that supports a conventional probate accounting. The executor does not have to prove post-death income because the assets were distributed to the trust before they could produce income. The trustee's signed receipt proves distribution of the entire estate to the trust, even when countless true beneficiaries receive a share from the trustee. If the trustee fails to get a receipt from the beneficiary of the photographs or if an unhappy child refuses to acknowledge receipt of tangible personal property, the court's review of the accounting is unaffected.

If a sale of real property is necessary or advisable, the trustee can sell unless the will prohibits a sale. Title to real property is vested in the trustee under the residuary clause. The executor need not petition the court for possession, custody or control of real property to obtain the power to sell. The value of the real property will not be included in determining the maximum executor's commission.

If the fiduciary's lawyer is paid from trust assets, the executor is relieved from petitioning for approval of attorney fees. If there are publicly traded investments in the probate estate, the executor can avoid the headache of investment accounting to the court. The probate accounting does not report dividends and interest produced after distribution of the investments to the trust. It does not report reinvestments and other purchases inside the trust with the necessary adjustment to the number of units and carrying value; nor sales inside the trust with the gain or loss and necessary adjustment to units and value; nor distributions of shares of each investment to the true beneficiaries at adjusted value.

The client can designate the trust as beneficiary of a life insurance policy or transfer-on-death account if the designation of true beneficiaries is too complicated for the financial institution to accept. The death benefit and TOD assets, because they pass to the trust rather than the estate, will avoid probate.

An unreasonable true beneficiary has no standing to intervene in the estate proceeding and must initiate a separate proceeding against the trustee to pursue a claim. (This coin has another side, though, where the beneficiary is reasonable or the fiduciary breaches a duty.)

Unless there is a caveat or other litigation involving the estate, probate should be easy no matter how difficult the trust administration is.

This approach does not relieve the trustee from delivering a complete accounting to the true beneficiaries. The beneficiaries, however, may waive trust accountings under N.C.G.S. Section 36C-8-813(c). If the preparation of a formal accounting will be expensive, a beneficiary might waive the accounting if the trustee provides sufficient documentation and satisfies the beneficiary that no breach of fiduciary duty has occurred.

The probate described above is not as easy as a summary administration. Accordingly, this approach should not be used by a married client who wishes to leave everything to his spouse. It also should not be used by a client who wishes to leave the entire estate to a single nonspousal beneficiary, provided that the beneficiary is also the executor. Such an executor can distribute the entire estate to himself soon after the decedent's death, assume the liabilities of the estate and achieve the same results described above.

The "pour-over-to-a-testamentary-trust" will has disadvantages. It appears more complicated than necessary, inserting a middle man between the executor and the true beneficiaries. Clients may not like the apparent complexity.

The executor-trustee cannot elect to treat the estate and trust as the same taxpayer. She may have to file an income tax return for the estate in addition to returns for the trust. The trust is stuck with calendar year reporting and consequences that fiscal year reporting might have avoided or mitigated.

The fiduciary may be tempted to claim double compensation, seeking the maximum executor's commission and also trustee compensation. A testator can prevent this by limiting or prohibiting executor compensation. Such a limitation should not be a deal-breaker because reasonable compensation is still available under the trust compensation statutes.
Title to the real property does not pass under the will to the true beneficiaries. Instead it passes to the trustee and the trustee must deliver a deed to the beneficiaries. If, however, the client does not want the fiduciary to have the power to sell real property, the client can achieve a direct transfer of title by specifically devising real property to the true beneficiaries.

The executor and beneficiaries lose the protections of probate court supervision. But the protections are not free. The expense explains, in part, the prevalence of revocable trusts.

I find that clients who see how the testamentary trust can reduce estate administration expenses tend to like it, despite the disadvantages. So I propose the plan to clients in situations where the client does not need or declines a revocable trust.

When drafting a pour-over-to-a-testamentary-trust will, I rely on the BB&T Estate Planning Forms Manual, using the Manual’s “Simple Will for a Married Person with Minor Children” (or “Will Form No. 2” in Part 2 of the Manual, beginning on page 3-25 of the 2016 edition). This form will qualify the estate for summary administration if the client is married and wishes to leave everything to the spouse. The form leaves the residuary estate to a testamentary trust (for the testator’s children) if the client survives his or her spouse. I change the form to:

1. Give the tangible personal property to the testamentary trust if the client survives his or her spouse (in Article I, Paragraph A of the form);
2. Remove the spouse as a beneficiary of the probate estate (in Article I, Paragraphs A and B of the form) if the client is unmarried or does not wish to leave everything to his or her spouse;
3. Rewrite the terms of the testamentary trust (Article II of the form) to distribute the assets, including the tangible personal property, to the true beneficiaries; and
4. Require the trustee to pay the estate’s liabilities.

As far as I can tell, the approach described above is not used much. There may be pitfalls I have not discovered yet. I hope that members of the Section will provide guidance and feedback.

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Pro Bono Corner

By David Silver

The NCBA’s 4ALL Statewide Service Day is a program that, for one day each year, gets attorneys to answer phone calls from the general public to answer their legal questions at no charge. The next 4ALL is scheduled for Friday, March 2, 2018. This program has existed for 10 years, and I have participated every year that it has been in Greenville. Here, the attorneys gather in a phone bank at a local television station. A 1-800 number is advertised on that TV station all day, and the station will occasionally show the lawyers answering phone calls, just like a telethon. The volunteer attorneys work the phones for one of four three-hour shifts.

The three-hour shift goes very quickly, and my ear is normally burning by the end of my shift as a result of the phone being pressed against it for almost the entire time. I would guess that I take about 35 calls during my shift, with the vast majority of the calls being related to Elder Law, Estate Planning and Estate Administration. If there is a question about a topic that I am not comfortable discussing (like criminal law), then I pass the phone to a lawyer who practices in that area, and if another attorney gets a questions related to Elder Law, they will frequently pass the phone to me. I find myself switching seats every few minutes, which is preferable to having phone cords wrapped around everyone’s neck.

The volunteer attorneys are not allowed to identify themselves to the callers, so this is not something to be done to try to drum up business. However, there aren’t exactly a lot of potential paying clients calling in - the phone calls are about what you would expect from a free legal service. Many of the calls are about things that we discuss everyday (Medicaid eligibility, estate administration), but from people who might not otherwise seek our advice (the people who are calling do not claim to have much in the way of assets). This represents a significant percentage of the calls received, and therefore I feel that it is particularly important that there is an Elder Law attorney present and available to help with these kinds of calls. Some of the calls are from people who have had random legal issues lingering in their minds for years but haven’t had the money to obtain a legal opinion (one guy kept talking about a claim that came about from before I was born). Some of the calls are just ridiculous, and these stories get shared among the lawyers whenever there is a lull in the phone calls. However, I have never had any caller be anything other than thankful, no matter if I was able to provide useful advice or had to tell them that their claim had no legal basis.

When my kids are grown and I have my practice running smoothly, I hope to be more involved in some larger pro bono efforts that reach numerous people in need. Unfortunately, I don’t have the luxury of dedicating that much time to these types of projects at this time of my life, so my pro bono activities are currently limited to helping individual clients. However, I can easily set aside three-hours once a year to answer legal questions over the phone, and this allows me to reach out to people outside of my individual sphere. I would encourage other Elder Law attorneys to consider participating in the next 4ALL Service Day.