Using Trusts to Own Real Estate – Part 1

By Dyches Boddiford

Trusts have been used as an entity to hold assets, such as real estate for hundreds, if not thousands, of years. Obviously, it's old stuff. But, with each generation's trials and tribulations, trusts evolve to meet new challenges.

High Taxes and aggressive litigation are today's motivators. Tax risks range from income tax to draconian death taxes that consume up to 55% of the assets a person leaves behind. Trusts are often used along with more modern adaptations of other old entities, such as partnership aberrations, to include family limited partnerships and limited liability companies. The quest is to keep what you have accumulated and to have some extended control of it, even after death.

A perfect example of using ingenuity to keep one's assets away from the grips of the tax man was a trust established by Maria Cristofani in 1984. Maria established a trust and transferred to it real estate with a value of $70,000. The primary beneficiaries were her two children and, as contingent beneficiaries, 5 grandchildren should the two primary beneficiaries die within 120 days of Maria. All was fine until Maria died and the IRS audited her estate tax return.

Naturally, the IRS wanted more money. They claimed that Maria failed to file a gift tax return and owed back gift taxes. The IRS argued that Maria was entitled to give $10,000 per year to the two primary beneficiaries, but that taxes were owed on the $50,000 not excluded. The estate disagreed, claiming that the 5 contingent beneficiaries did have an interest in the trust. The trust had a Crummey power and, in accordance with that power, the trustee had given written notice to all 7 beneficiaries of their right to withdraw. Thus, the full $70,000 was excludable.

This means that multiple-beneficiary trusts now can be used to expand the fit-tax exclusion. It took someone with a tolerance for risk to mix old law, and an old trust entity with a new way of looking at the old to save Maria's family substantial wealth.

Over the years trusts have been used extensively in the attempt to control how much the government inherits. Some of the more familiar trust names include: Bypass Trust; Marital Deduction Trust; Generation Skipping Trust; Grantor Retained Income Trust; Insurance Trust; etc. The common thread for all of these trusts is to legally avoid paying the majority of the deceased's wealth to the government. Failure to act is to assure that the estate will pay the highest possible tax.

A NEED FOR PRIVACY

Real Estate Investors often use trusts as business devices. It is hard persons never being in business to understand, but business can be war. There is an ever growing number of enemy soldiers attempting to invade and plunder the investor's castle of wealth. Sometimes this is accomplished by out and out illegal means, such as thieves that rob and destroy property or

those who embezzle by not paying rent. The cruelest enemy is he who uses the law to plunder. Today, lawsuits are treated as a lottery.
Enemy troops look for excuses to sue; it is nearly a guaranteed profit. If a person can find some excuse to sue, even if very flimsy, the defendant will almost always settle for at least a few thousand dollars because it is cheaper to settle than to incur the cost of legal defense. It has become so bad that in some cities, such as Buffalo, NY, unscrupulous people publish lists of landlords and divulge such things as the number of properties, the number of units and the total value of real estate owned. Why? Because contingency fee lawyers will not spend the time and money to go after someone with minimum assets. They look for the ‘fatted lamb’.

LAND TRUSTS

A result of this attack is a defense system. Trusts are used by some investors as a key part of their defense. The most common trust used in real estate investing is referred to as an Illinois style land trust. The primary purpose is to remove the legal title from the investor’s name. The title is held in the name of a trustee and the investor is both the grantor and the beneficiary to the trust. the trust does not offer the same kinds of protection a corporation or limited liability company can, but it has a place in the castle’s defense and is the most economical of all entities to set up and maintain.

Legal advisors often recommend trusts be used in conjunction with other business entities assuming the amount of wealth involved is sufficient to justify the cost of the business entity. Trusts, on the other hand, are usually very economical. An attorney prepares the original trust and it can be duplicated for additional use. The fee to have a knowledgeable attorney prepare a land trust can range from $300 to $1,000. Some of us do our own trusts, but a great deal of knowledge must be obtained before you consider doing this. There are no additional expenses, such as franchise fees or income tax returns. A land trust is reported on the beneficiary’s tax return as if the beneficiary personally owned the property.

On August 26 & 27, 2017, Dyches Boddiford will present a 2 day Seminar in Greenville on Using Trusts in Your Real Estate Business. **Read More an register for this event at: UpstateCREIA.com/TrustReg**