Trust Me: The Dirt on Trust Ownership of Real Estate

By Mindy H. Stern

INTRODUCTION

So, a client walks into a bar (association) expressing an interest in transferring real property into a trust. How should you respond? When is a trust appropriate, or when is an LLC the better approach? This article will help you ask that client the right questions, provide an overview of several types of trusts and the various purposes they serve, and identify issues you should address with your clients to help them achieve their goals.

OVERVIEW—PURPOSE AND TYPES OF TRUSTS

Revocable Trusts

A revocable trust, also often referred to as a living trust, is a contract between the creator of the trust (the grantor) and the named trustee. It typically is created to avoid the expense and possible delay of probating a will, to make it easier and less expensive to create and administer additional family trusts to be created after death, and to provide an orderly way to manage the grantor's financial affairs if the grantor becomes disabled or incapacitated. It is a useful tool to avoid the ancillary probate of real property located in jurisdictions other than the one where the grantor is domiciled. It also can avoid probate in the state of domicile if it contains the grantor's plan for the ultimate disposition of his or her assets, although it does not cut off a surviving spouse's right of election under New York Estates, Powers and Trust Law (EPTL) Section 5-1.1-A (b)(1)(F) with respect to the property. Real property (and cooperative apartments, if the cooperative corporation permits it) can be transferred to a revocable trust or purchased and sold by a trustee after the grantor transfers the property to the trust.

However, because the trust is revocable and amendable, for tax purposes there is no completed gift. So, despite common client misconceptions to the contrary, *revocable trusts do not save estate or income taxes*. And transferring real property from a joint tenancy or a tenancy by the entirety may create a gift tax issue.

Irrevocable Trusts

Unlike revocable trusts, transfers of property to an irrevocable trust are deemed completed when the transfer is made. Tax savings and other benefits can be achieved through different types of irrevocable trusts.

Qualified Personal Residence Trust (QPRT)

Qualified personal residence trusts (QPRTS) are trusts authorized by Internal Revenue Code (IRC) Section 2701. A personal residence (either the principal residence, or one other residence) is transferred into an irrevocable QPRT.[1] To qualify as a personal residence, the property cannot be occupied by anyone other than the creator of the QPRT or the grantor's spouse or dependent.[2]

The creator of the QPRT has a right to use the residence for a fixed term. When the term ends, the residence passes to designated beneficiaries, or continues to be held in further trust for their eventual benefit. During this initial term, the grantor's payment of interest on any loan secured by the real estate, or any rent payable in connection with it (including monthly maintenance payable to a cooperative corporation, or common charges payable to a condominium association), is not considered a gift, and the trust creator can continue to take those payments as deductions on his or her personal income tax returns; but the payment by the trust creator of mortgage *principal* constitutes a gift. [3]

The transfer of a residence into a QPRT is a gift of a future interest, because the beneficiaries won't receive it until the trust term ends. The value of the gift is, therefore, less than it would be if the property was transferred to the beneficiaries today. The value is determined actuarially according to IRC § 7520, taking into account: (1) the present value of the property; (2) the length of the trust term (the longer the term, the lower the value of the taxable gift); (3) the age of the trust creator; and (4) the interest rate then used by the IRS in its actuarial tables.

A QPRT works well for property likely to appreciate in value during the grantor's remaining life, because it removes that future appreciation from the grantor's estate. But there are two important caveats.

First, the trust creator must survive the term to take advantage of the tax benefits.[4] Otherwise, the value of

---

Mindy H. Stern, Esq., is an attorney at Schwartz Sladkus Reich Greenberg Atlas LLP. The author gratefully acknowledges the assistance of Charles Farrell, senior staff member, *St. John's Law Review*, *Journal of Catholic Legal Studies*, St. John's University School of Law, candidate for J.D., 2019; Dana Kahati, member, Fordham Law Real Estate Society, Fordham University School of Law, candidate for J.D. 2020; Gerald Antetomaso, Esq., Evans Fox LLP; Marvin Bagwell, Esq., vice president and chief New York State Counsel, Old Republic National Title Insurance Company; Kristen V. Bellouny, Esq., chief underwriting counsel and executive vice president, Kensington Vanguard National Land Services of NY LLC; James D. Burnham, CPA, CEO, Go!Accountants, Inc.; and Scott Nadler, loan consultant, Loan Depot, in connection with the preparation of this article.

the residence at the grantor's death is included in the grantor's estate as though the trust was never created. If this is a concern, the trust creator can (if insurable at acceptable rates) purchase a term life insurance policy in the face amount of the estate tax payable if the trust creator does not survive the term. If the insurance is purchased by, and placed in, an irrevocable insurance trust, the proceeds can be eliminated from the estate. To reduce costs, the insurance can be purchased during the last year or two of the term.

Second, if the grantor wishes to remain in the residence after the term expires, the trust cannot require the beneficiaries to consent, and must explicitly prohibit a sale of the residence back to the trust creator.[5] In addition, the grantor must pay fair market rent to the then owner of the property (the beneficiaries if they acquired title outright, or the trustee of the trust if the property remains in further trust for the grantor's lifetime). But this rental stream can (and should) be viewed as another way of transferring wealth to the ultimate property recipients. It is common practice for the trust creator to continue to use and enjoy the residence pursuant to a written occupancy agreement until the grantor's death.

Medicaid Asset Protection Trusts

Medicaid asset protection trusts (MAPTs) are increasingly popular for families with modest means. They protect the equity in a family residence from being depleted to pay for nursing home care for the elderly relative residing in it. The Medicaid program in New York currently has a five-year lookback period for asset transfers made by the trust grantor prior to the grantor's application for nursing home care. Different look-back rules apply for in-home care. MAPTs often are recommended by elder care attorneys, for several reasons. They protect the residence not only for purposes of qualifying for Medicaid without exposing the home equity from claw back, but also from other creditors and relatives with self-interested ulterior motives. The grantor can continue to live in the home after the transfer. If the trust permits, the trustee can sell the existing home without any documents having to be signed by an often mentally incapacitated grantor, and either purchase another residence for the grantor, or if the grantor relocates to a nursing home, preserve the net proceeds in trust to supplement, rather than supplant, the government benefits then being received by the grantor. Because the grantor's gift of the property to the trust is considered an incomplete gift for estate and gift tax purposes, the lifetime capital gains tax exclusion for a homeowner's principal residence usually is preserved, keeping in mind, as is generally the case, that if some portion of the property is used for other purposes, this could affect the exclusion amount, and if the transferred property remains in the trust at the time of the grantor's death, for income and estate tax purposes the trust beneficiaries receive it with a stepped-up income tax basis.

If the senior was receiving STAR, veteran or other property tax exemptions, these continue after the transfer to a MAPT. These and other exemptions are discussed in more detail below.

Even though the trust is irrevocable, which typically triggers a need for the trust to become a separate taxpaying entity with rates identical to individuals but which ratchet up to the highest brackets more quickly, if the MAPT is drafted as a "grantor trust," income generated by trust assets is taxed at the individual grantor's income tax rates on the same rate schedule for individuals, rather than trust rates.

Testamentary Trusts (created post-death, either in a Will or a Living Trust)—A testamentary trust is one created in the will of the property owner, which takes effect upon his or her death. The typical purpose of a testamentary trust created to hold real estate is to permit one family member to use or occupy it, or, if it is income-producing property, to receive the financial benefits of the property, during his or her life, or for some other specified term. When the term ends, the property typically is transferred to other family members, friends or charity. This is a common second marriage scenario, where the grantor wants a surviving spouse to be able to occupy a residence or vacation home for life, or until he or she no longer wants or is able to do so, and to then transfer the property to the children of a first marriage. It can (and often is) also used for commercial property where the owner wishes to control who among multiple generations receives the economic benefit of the real estate. Transfers of real property to a testamentary trust may or may not save estate taxes, depending upon the testator's overall estate plan.

Credit Shelter Trust—Married couples often establish trusts described as "credit shelter" or "by-pass" trusts. The purpose of this trust is to enable the surviving spouse (and sometimes other family members too) to use and enjoy the property in the trust during the spouse's lifetime without losing the benefit of the lifetime estate tax exemption amount available to the first spouse to die under federal or state law, depending on how the trust is drafted (hereafter referred to in these materials as the "Applicable Exclusion Amount"). The credit shelter trust can only be funded with property individually owned by the first spouse to die (with no designated beneficiary transferring the property, post death, to one or more third parties outside the deceased spouse's will), or with that spouse's interest in property owned as a tenant in common with others.

Qualified Terminable Interest Property (QTIP) Trusts—Married couples also often use the QTIP trust to achieve estate tax benefits while protecting property against the claims of possible creditors and second spouses. The QTIP allows assets (in a common estate plan, assets in excess of the Applicable Exclusion Amount being held in a credit shelter trust) to be held by a trustee for the benefit of the surviving spouse during his or her lifetime, free of estate and gift tax, with the remainder passing to named beneficiaries after the surviving spouse's death. Although a QTIP can save estate taxes, at the death of the surviving spouse the remainder is subject to estate tax, the net effect of which may be a deferral rather than an elimination of estate tax on the combined assets of the couple.

As is the case with all estate planning techniques, whether a credit shelter trust and/or QTIP trust is appropriate for a married couple will depend upon the circumstances of each situation.

Qualified Domestic Trusts for Non-Citizen Spouses—Spouses who are not U.S. citizens do not have an unlimited marital deduction.[6] Effective January 1, 2019, IRC § 2523(i)(2) permits an annual exclusion of $155,000 for transfers to non-citizen spouses—the same limit for post-death transfers to non-citizen spouses qualifying for the marital deduction. This amount—hereafter referred to as the "Non-Citizen Spouse Annual Exclusion Amount"—is indexed annually for inflation. To transfer more than $155,000 in 2019 to a non-citizen spouse, a citizen spouse must create a "qualified domestic trust" (QDOT) in the citizen spouse's will or a trust intended to serve as a will after death. The trust must comply with the provisions of IRC § 2056A which requires, among other things, that the trustee of the QDOT be a U.S. citizen.

So, if a citizen spouse and a non-citizen spouse jointly purchase real estate, and the non-citizen spouse does not contribute equally to the purchase price, the gift tax implications must be considered. For example, if the couple purchases property for $1 million, and the citizen spouse contributes $800,000, and the non-citizen spouse contributes $200,000, the citizen spouse will be deemed to have made a gift to the non-citizen spouse of $300,000 (the difference between $200,000 and $500,000, half the value of the property). Applying the Non-Citizen Spouse Annual Exclusion Amount for a gift to a non-citizen spouse, only $155,000 of the $300,000 gift would be tax exempt. So, the citizen spouse would be required to file a gift tax return and the citizen spouse would be using up $145,000 of his or her Applicable Exclusion Amount (the difference between the $300,000 gift and the $155,000 Non-Citizen Annual Exclusion Amount).

LIMITED LIABILITY COMPANIES

Limited liability companies are creatures of statute. New York's Limited Liability Company Law ("LLC Law") was enacted in 1994. Since then LLCs have become a common way to own real estate, especially what are typically referred to as a "single purpose entity"—an LLC formed solely to own a single piece of real estate. Section 609 of the LLC Law limits the personal liability of its members, managers and agents without their express written consent (such as personal guarantees and other contractual agreements) except as expressly set forth in the LLC's articles of organization, or for the member's fraudulent or other wrongful conduct under circumstances in which a court would permit the corporate veil to be pierced, or if a member/manager breaches his or her fiduciary duty to fellow members/managers. Single-asset LLCs also limit the liability of the entity itself to matters arising from or related only to that property, instead of multiple assets. As the New York State Supreme Court noted in *Spota v. White*, an LLC is "the hallmark of an investment in real estate and is used to limit personal liability." [7]

One of the key advantages to entity ownership for real estate in estate planning is the ease with which transfers can be made. Rather than needing to prepare, sign and file deeds each time the original owner (or any subsequent owner) wishes to transfer an interest in the property, a simple unrecorded gift letter or assignment of interest, coupled with updating the entity's membership interest records, can be executed. Depending upon the jurisdiction and the interest being conveyed, city or state real property transfer tax returns may need to be filed, and transfer tax may need to be paid, at the time of the conveyance.

Another key advantage is the convenience by which management planning and restrictions on transfer can be achieved. It is customary for management responsibilities to lie within the control of a single member or manager, and for transfers (either at the death of a member, or at the member's election) to be restricted to family members. So, LLCs provide a convenient way, for example, to retain and manage a valuable vacation home or family investment property for the benefit of subsequent generations.

TRUSTS VS. LLCS AS AN ESTATE PLANNING TOOL

Personal Liability

We already discussed LLCs. What about trusts? EPTL Section 11 describes the powers, duties and limitations of trustees. For example: they can be surcharged and removed as trustees if they co-mingle trust funds with their own assets.[8] It is against public policy under Section 11-1.7 if trustees fail to exercise reasonable care, diligence and prudence in carrying out their duties. A trustee who fails to comply with the Prudent Investor Act (Section 11-2.3) also risks surcharge and removal.[9] And if a trustee abuses his or her discretion in a dishonest, arbitrary or capricious manner, a court might require the trustee to pay from personal assets what is needed to rectify the abuse.[10] That said, trusts typically contain provisions exonerating trustees from personal liability if

Continued on page 18

Trust Ownership

Continued from page 15

trust assets depreciate or shrink in value absent a showing by affirmative evidence that the trustee failed to act within the scope of the trustee's authority, failed to exercise reasonable care, diligence and prudence, or failed to be impartial as to all interested parties.

Creditor Protection

As previously discussed, an LLC affords broad creditor protection with limited exceptions. A revocable trust does not, because the assets transferred to it are treated for these purposes as available to creditors. An irrevocable trust created with a debtor's assets is subject to being set aside as a fraudulent conveyance. But an irrevocable trust created with the assets of a third party is not available to the creditors of a trust beneficiary who has no discretion or control over the assets.

Avoiding Probate/Estate Administration

If someone domiciled in New York dies owning real estate located in another jurisdiction with no co-owner as joint tenants with rights of survivorship or as tenants by the entirety, an ancillary proceeding typically is required in the other jurisdiction in order for the New York Surrogate's Court-appointed estate executor (if there is a will) or administrator (if there isn't) to have the power to transfer the property, either to the recipients entitled to it under the will or by intestacy, or to a third party if it is being sold. Some jurisdictions vest immediate ownership in the heirs at law, and sometimes a title company is willing to insure a transfer without an executor or administrator being appointed if provided with sufficient proof that there are no heirs at law other than those requesting the transfer (this is a non-starter if the will contains different specific legatees or devisees different from the heirs at law), no creditors, and no estate or income tax liabilities. But even when that is the case, or if there is no title insurer involved, there may be other third parties (such as a lender or a cooperative corporation) who demand ancillary probate or administration.

Ancillary proceedings can be avoided by holding title to the real estate in the following ways: (1) with one or more joint tenants with rights of survivorship or by a married couple as tenants by the entirety; (2) in an LLC or other corporate entity; or (3) in a trust. But there are other estate planning and income, estate, and gift tax consequences to each of these decisions, discussed elsewhere in this article, which need to be considered before selecting which method of avoiding an ancillary probate or administration proceeding best serves the needs and goals of each client.

Insurance

Insurers of commercial property usually are comfortable with entity or trust ownership. They are more concerned about the nature of the building and improvements located on, and types of activities being conducted on, the premises, and assess insurable risks accordingly. Residential property is different. Some insurers will not underwrite residential property owned by an entity or trust, because they don't consider it "owner occupied" as they do when the property is individually owned, even when you explain that the transfer is for estate planning or other purposes and does not impact how the property is used. So be proactive and confer with the client's insurance company before final decisions are made. If the client needs to find a more receptive insurance company, the sooner this is addressed the better, as it might affect the timing and cost of the transaction.

Property Tax Issues (STAR and Other Exemptions)

Clients who own residential property often benefit from certain real property tax exemptions or abatements. New York has a veritable alphabet soup of possibilities available in various jurisdictions. Following are some examples, not intended to be an exhaustive list: STAR, Enhanced STAR, Veterans Exemptions, Senior Citizen Homeowners Exemptions, Disabled Homeowners Exemptions, Clergy Exemptions, Disabled Crime Victim/Good Samaritan Exemptions, SCRIE, and in New York City, the Cooperative and Condominium Property Tax Abatement Credit. Before transferring property benefiting from one or more of these abatements or exemptions, you need to confirm that the client will not lose them. A client might decide to proceed with the transfer anyway, but I believe in the "no surprises" rule when it comes to client relations, and you should too.

The most common is the STAR (School Tax Relief Program) created by § 425 of the New York Real Property Tax Law (RPTL).[11] New Yorkers who own and reside in one, two or three family homes, condominium units or cooperative apartments as their primary residence are eligible for these partial abatements on their property taxes. Transfers of the property to a revocable trust still qualify for the STAR abatement if the property is the primary residence of the trustee or trust beneficiary. This also is true for the NYC Cooperative and Condominium Property Tax Abatement Credit under § 467a of the RPTL. But transfers to an LLC or other corporate entity are ineligible for the STAR abatement, even if the homeowner is the sole member of the entity and occupies the property as his or her primary residence, unless the property is a qualifying farm.

Enhanced STAR is available under § 425 of the RPTL to seniors (65 and older) who own and live in their primary residence and meet certain income requirements.

The same eligibility requirements regarding trusts and LLCs as they relate to the STAR program apply here.

There are several types of veterans' exemptions available under §§ 458-a and 458-b of the RPTL for residential property owners who rendered military service to the U.S.[12] The eligibility requirements vary, as do the ways the exemption amount is computed. These exemptions are available to shareholders and unit owners of coops and condos who otherwise meet the eligibility requirements. Transfers to trusts qualify for the abatement provided the owner eligible prior to the transfer is the trustee or beneficiary of the trust. Although we were advised by a representative of the NYS Department of Taxation and Finance (NYSDTF) in a telephone call that transfers to LLCs are treated the same as trusts, the statute and the Department's application forms and instructions are silent as to the eligibility of LLCs or other entities for these exemptions, so it would be prudent not to rely upon that advice and assume that there is no available abatement, even if the homeowner/veteran is the sole member of the LLC or sole shareholder or partner of other corporate entities and occupies the property as his or her primary residence.

Disabled homeowners are eligible for additional property tax abatements if they meet certain requirements. The property must (1) be used solely for residential purposes (otherwise the exemption is available only for the portion used for residential purposes), (2) be the "legal residence" of the disabled person, and (3) be occupied by that person unless he or she is receiving medical treatment at a facility. A trust can own the property if all the beneficiaries qualify for the exemption. Transfers to an LLC are ineligible for the disabled homeowners' abatement, even if the homeowner is the sole member of the LLC and occupies the property as his or her primary residence.

There is a Disabled Crime Victim/Good Samaritan Exemption under § 459 of the RPTL available for one, two or three family homeowners who become physically disabled because of a crime.[13] The home must have been improved to make it handicap accessible, and the improvements must enhance the property's value. The increase in the value attributable to the improvement is exempt from property tax. The statute and NYSDTF application documents are silent as to the eligibility of trusts and LLCs for this exemption, so it is prudent to assume they are not.

In addition to property tax exemptions granted to eligible not-for-profit entities under § 420a of the RPTL, there also is an exemption under § 462 of the RPTL for property owned by a religious organization and used as a residence for its clergy, provided various eligibility requirements are met. In addition, § 436 of the RPTL exempts from property tax residential property held in trust by and occupied as a residence by clergy for the benefit of congregation members if the clergy is actively engaged in the work of the denomination and the property otherwise meets the eligibility requirements under 420a; and § 460 of the RPTL grants a property tax abatement of up to $1,500 to clergy who occupy a residence while actively engaged in the work assigned by the congregation or who are unable to do so either because the clergy is over 70, or suffering from impaired health. The un-remarried spouse of otherwise eligible clergy can continue to receive this abatement. The exemptions under §§ 436 and 460 are not available for transfers to LLCs or other corporate entities owned by otherwise eligible clergy.[14]

Financing

It is standard operating procedure for commercial property, often income producing, and sometimes the site of business operations (industrial, office, retail, mixed use) to be purchased by "SPEs" (single purpose entities), which typically (but not always) are LLCs. Commercial lenders are both accustomed to and comfortable with such arrangements, usually requiring guarantees from principals and other collateral they deem sufficient to secure the loan repayment.

Conversely, financing the purchase of residential property in an entity or a trust has its challenges. Fannie Mae doesn't allow either. That leaves jumbo loans made by portfolio lenders, credit unions and others who don't sell their loans on the secondary market as the only lenders. As to those, each lender is likely to have its own underlying guidelines which should be ascertained as soon as your client tells you that he or she is considering buying, financing or mortgaging property owned individually through a trust or similar entity. Mortgages typically have due-on-sale clauses that are drafted broadly enough to include "mere change of identity" transfers of title. Although the federal Garn-St. Germain Depository Institutions Act of 1982 (12 U.S.C. § 226) prohibits lenders from denying consent to a transfer from an individual to that individual's intervivos revocable trust, the current mortgagee holding a mortgage with a due-on-sale clause will most likely treat all other transfers as being subject to its consent, triggering an application process that essentially is a full refinance.[15]

In my experience (which isn't necessarily dispositive), lenders willing to entertain entity ownership of residential property don't favor LLCs over trusts, or vice versa. The key consideration for a trust is whether it is revocable (typically acceptable) or irrevocable (typically not, because of concerns about the trust assets being unavailable to creditors). Other considerations also come into play. In the case of an LLC, that might include, for example, how many members are in the LLC, who they are, and their connection to the real estate. For a trust, often the bank will require the grantor and at least one of the trustees to be the borrower. So, if the proposed title holder is an LLC or a trust, the key take-away here is to address the financing issue right away with the client's mortgage broker or prospective lender, to determine what approvals are required, and what choices are available.

Income Tax

Unless you are a CPA or tax attorney who regularly deals with income tax issues relating to real estate, my first (and probably most important) advice is to bring your client's tax advisor into the planning process early on. Every client has their own income tax issues and deciding whether to form an entity or create a trust to hold title to real estate cannot be done in a vacuum. Each has tax consequences and making the wrong decision could cost your client time, money and aggravation.

That said, there are a few basic considerations to be aware of. First, if there is only one member of an LLC, it is treated for income tax purposes as a "disregarded entity" and there is no double taxation—meaning, no tax at the entity level. If there are multiple members, the LLC will be treated for income tax purposes as a partnership, unless the members elect otherwise.

Second, sometimes the right entity choice is an S-corporation rather than an LLC, because depending upon where the property is located, and where the entity is conducting business, and whether the entity is holding title passively to non-income producing property, or actively managing property generating significant income, there could be self-employment tax for an LLC, but not for an S-corp. Again, the client's tax advisor should help you evaluate this.

If the trust is a revocable trust, it is treated for income tax purposes as a "disregarded entity" (same as a single member LLC) and there is no double taxation—meaning, no tax at the trust level.

If the trust is an irrevocable trust, it must obtain its own EIN and is treated as a separate entity for income tax purposes. Unless the trust provides otherwise, income generated by trust assets is taxable to the trust, subject to some complicated rules regarding trust distributions that are beyond the scope of this discussion. As mentioned in the discussion about MAPTs, trust income tax rates currently are identical to personal income tax rates, but accelerate to the higher brackets faster, and sometimes the trust is intentionally drafted to attribute all trust income to the grantor—the trust creator—as a way of making additional lifetime gifts to the ultimate beneficiaries.

It is essential to evaluate how best to achieve each client's goals regarding their real estate in the context of their overall estate, gift and income tax planning.

Amendments to Governing Documents

Single-member LLC documents and revocable trust documents can both be amended easily.

Multi-member LLC documents can also be amended easily provided the requisite number of members as provided for in the original governing documents agree or if there is no applicable provision in the governing documents, provided the requirements in the governing limited liability company law are met.

Under EPTL 7-1.9, irrevocable trusts cannot be revoked or amended without the written, signed and acknowledged consent of the grantor and all the beneficiaries. Court approval is required when some of them are minors.[16] If the trust by its terms also requires the consent of the trustee, that too is required unless a court determines otherwise. *See* for example *Elser v. Meyer*, 29 A.D.3d 580, 814 N.Y.S.2d 684 (2d Dep't 2006) where the appellate court returned the case to the supreme court to determine if the trustee unreasonably withheld his consent.[17]

Because of these constraints, well-drafted trusts provide discretion to the grantor and/or trustees in certain scenarios, and if federal and governing state law is complied with, their decisions are likely to be upheld. For example, sometimes the trust will allow the grantor to remove and replace trustees or allow trustees to appoint successors (although this still requires court approval if the trust is a testamentary trust), or allow trustees to use the governing law's "decanting" statute (if there is one) to transfer the trust assets into a new trust containing different administrative provisions intended to fix problems or address omissions in the existing trust. The "decanting" statutes are different, so you would need to research the applicable law to evaluate what discretion trustees have to extend the trust term, change beneficiaries or their respective interests, or make other key changes. New York's "decanting" statute is in 10-6.6 of the EPTL.[18]

Administrative Costs and Burdens

LLCs are relatively easy to form. In New York, pick an available name, file articles of organization with the New York Secretary of State's Office pursuant to § 203 of the LLC Law, select the method by which the entity elects to be taxed, and off you go, with one significant caveat. Section 206 of the LLC Law requires an LLC to publish, within 120 days of its formation, notice of the formation in two general circulation newspapers designated by the county clerk in the county where the LLC was formed for six consecutive weeks. If you think you can get around the publication requirement by selecting a less expensive newspaper in another county, forget it. That's illegal. Another often tried, equally ineffective approach is forming the entity in another jurisdiction (Delaware or one of the Dakotas often are selected because they are perceived as more hospitable to entities and creditors prefer the bankruptcy-related protections in the Delaware LLC statute) and then not qualifying to do business in the state where the property is located. Part of the qualification process in New York is fulfilling those publication requirements. There are no publication requirements for corporations in New York.

Once formed, New York LLCs as well as foreign entities qualified to do business here have reporting and biennial registration fee requirements. This is, of course, in addition to any income tax reporting requirements. Maintaining a separate bank account and not co-mingling corporate and personal assets and expenses are prudent ways to confirm that members are preserving the corporate formalities needed to withstand efforts to pierce the corporate veil. So, there is an ongoing cost associated with forming and maintaining an entity in New York.

On the other hand, trusts do not have such formation requirements. The due execution of the trust indenture is sufficient to create it. If it is irrevocable, obtain a separate tax ID number for it, and comply with the tax reporting requirements.

But before you abandon LLCs because of these costs, consider this: the sole member of an LLC is not answerable to anyone else for actions taken on behalf of the entity. Members of a multi-member LLC (or the managers, if it is manager-managed) are answerable to each other, but not to outsiders unless they contractually agree to be (lenders being the prime example). On the other hand, trusts come with special statutory obligations to account to trust beneficiaries. If the trust is revocable, and the grantor is the sole trustee, those obligations are minimal because the grantor can revoke or amend the trust whenever he or she likes. If there is a co-trustee, the revocable trust can (and often does) permit the grantor to continue to control how the trust funds are invested and distributed unless and until the grantor becomes incapacitated. But once that happens, or if the grantor dies, or if the trust was irrevocable when formed, the trustees have a fiduciary duty to the beneficiaries. The trust indenture can permit the trustees to decide not to provide annual accountings or judicial accountings, and limit trustee liability to "bad boy" acts, but none of those clauses completely absolve trustees of all liability, as previously discussed.

So, when helping a client select which type of entity or trust works best, the administrative costs and burdens of each should be discussed, so that the client makes an informed decision. Again, the key is avoiding post-decision surprises.

SPECIAL CONSIDERATIONS FOR COOPS

Transfers of cooperative apartments to entities have become increasingly more common since the laws previously creating adverse tax consequences were changed, and as shareholders have become more sophisticated about estate planning and pressure Boards of Directors to be more flexible. Boards have two primary concerns—who is occupying the apartment, and who is financially responsible for paying shareholder obligations. These typically are addressed in occupancy agreements and personal guarantees prepared by counsel to the cooperative corporation and signed by the shareholder requesting the transfer to the trust. The corporation also usually requires any further transfers from the trust to the ultimate beneficiaries to be subject to further Board approval when the event triggering the trust termination (often the death of the trust grantor/original shareholder) occurs.

TITLE ISSUES FOR TRUSTS

When underwriting title for a transfer to a trust, title companies typically ask for a complete copy of the instrument creating it, for several reasons.

1. If the trust was created during the grantor's life, the title company needs to confirm it was properly executed by all necessary parties in accordance with EPTL 7-1.17.[19]
2. If the trust is a testamentary trust created in the grantor's will after death, the title company needs proof that (1) the will was admitted to probate by a court of applicable jurisdiction (in New York, the Surrogate's Court located in the county where the decedent was domiciled); and (2) a trustee was appointed by the court, any successor trustees now serving were court-appointed, and the current trustee's appointment was not revoked.
3. Whether lifetime or testamentary, the title company also needs to confirm that the instrument creating the trust gives the trustee the power to acquire and convey real estate without restriction, or, if it is silent as to that power, that the law governing its formation does not require this power to be contained in the trust instrument. The title company will need a complete copy of the trust, including all amendments.
4. If there are judgments and liens against the grantor of a revocable trust, they attach to assets in the trust, so they must be cleared for the trustee to convey title to real estate owned by the trust.
5. The title company probably will want an affidavit from the trustee confirming (1) that the trust was in full force and effect when the property was transferred to it, (2) that it remains in full force and effect at the time the trustees are conveying it from the trust, and (3) that the trustee has the authority under the trust instrument to convey and acquire property.
6. If there is more than one trustee, the trust must be reviewed to confirm whether all trustees must sign, or if the signatures of a single trustee or a majority are sufficient.

If there are trusts in a chain of title, the title company may need to confirm that each of those trusts were in full force and effect when the property was transferred from them, unless the deeds were recorded six or more years ago.

There may be other provisions in the trust instrument which require further inquiries and underwriting, such as a limited power of appointment given to the grantor to select beneficiaries, or a life estate granted to the grantor or others, and, depending upon the type of trust and the grantor's retention of certain powers or beneficial interests, if the grantor has died, federal and state estate tax lien clearances.

Deeds from trusts must cite full consideration, and the trust must have a tax ID number – either the grantor's social if the trust is revocable, or a separate EIN if the trust is irrevocable.

The proper manner for trusts to hold title is in the name of the trustees, not the trust. Example: "John Doe and Jane Doe, or their successors, as trustees of the Doe Family Trust u/a/d July 28, 2018," not "The Doe Family Trust."

Trustees cannot delegate their fiduciary duties, so they must either pre-sign conveyance documents or attend a conveyance closing.

CONCLUSION

When considering whether to recommend to a client that real estate be acquired by or transferred to a trust or an LLC, it is essential to first understand the client's goals and the nature and intended use of the property. It is equally important to bring the client's other professional advisors into the discussion—their insurance consultant, tax advisor, title insurer, estate planning counsel and possibly their personal financial advisor. Entity ownership (including trusts) can limit personal liability, achieve valuation discounts, and control who is entitled to use and enjoy the property, and receive its economic benefits. But as is always the case with proper planning, each client situation must be evaluated on its own merits to determine the most appropriate planning tools. Some clients are more reluctant to give up the control required to achieve substantial tax benefits. Aggressive tax planning must always be weighed against each client's other needs and desires, to achieve a proper balance between preserving wealth for future generations and allowing current owners to enjoy their assets (and the economic benefits of those assets) during their own lifetime. And all the considerations described in these materials should be discussed before deciding which options best serve the needs of the client and the client's family, now and in the foreseeable future.

Endnotes

1. Treas. Reg. § 25.2702-5(b)(2).
2. Treas. Reg. § 25.2702-5(b).
3. *See* N.Y. Est. Powers & Trusts Law 11-2.1(1)(1)(A) (McKinney); *see also* PLR 9249014, (I.R.S. Sept. 4, 1992).
4. IRC § 2036.
5. Treas. Reg. 25.2702-5(b).
6. IRC § 2056A; IRC § 2523.
7. *Spota v. White*, 997 N.Y.S.2d 101, 101 (Sup. Ct. 2014).
8. EPTL 11-1.6 (McKinney).
9. EPTL 11-1.7, 11-2.3 (McKinney).
10. EPTL 11-2.3-A (McKinney).
11. N.Y. Real Prop. Tax Law § 425 (McKinney).
12. RPTL § 458-1, 458-b (McKinney).
13. RPTL § 459-b (McKinney).
14. RPTL § 436, 460 (McKinney).
15. Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97- 320, 96 Stat. 1469 (codified as amended in scattered sections of 12 U.S.C.), codified in 12 U.S.C.S. § 1701j-3(d)(8).
16. *See, e.g., In re Mainzer*, 151 Misc.2d 203, 206, 573 N.Y.S.2d 129 (Sur. Ct. N.Y. Cty. 1991); *In re Johnson*, N.Y.L.J, June 3, 2011 at 30, col 1 (Sur. Ct. N.Y. Cty. 1986); *In re Silverstein*, N.Y.L.J., May 28, 2009, at 41, col. 5 (Sur. Ct. Kings Cty. 1986).
17. *See, e.g., Elser v. Meyer*, 29 A.D.3d 580, 581, 814 N.Y.S.2d 684 (2006) (where the appellate court returned the case to the supreme court to determine if the trustee unreasonably withheld his consent).
18. EPTL 10-6.6 (McKinney).
19. EPTL 7-1.17(a) (McKinney).