

Don't Let Your Plan Fail: Why Reviewing Your Trust is Critical

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Revocable trusts are often the centerpiece of a client's estate plan for the many benefits that they provide. Revocable trusts are private agreements that are easily amendable, and avoid the costs and delays associated with probate. They ensure the management of assets in the event of a client's incapacity and, at death, a seamless transition of assets to the client's intended beneficiaries.

However, even the most carefully drafted and intricate trust agreement will be ineffective if it is not implemented correctly.

A revocable trust is essentially an empty shell until it is funded with assets. Advisors and legal counsel will likely take steps to ensure that all of a client's non-retirement assets are transferred or retitled into their revocable trust at its inception. When assets are later acquired, they must be transferred into the trust to be effective. In the best circumstances, assets that remain outside the trust will necessitate probate, incurring administrative costs and delays that the client sought to avoid by establishing the revocable trust. At worst, failing to properly title or convey assets into the trust may result in the imposition of avoidable taxes and the wrong beneficiaries receiving assets.

Why Proper Trust Funding Matters

Many clients presume that listing an asset on a schedule included with their trust is all that is required to transfer assets into their trust. In reality, assets must be formally transferred to the trust, or the trust must be listed as the beneficiary of any assets that remain outside the trust, for it to be effective. Some assets, such as bank or brokerage accounts, can be easily retitled and transferred into a trust. Other assets require the preparation of formal legal documents to effect the transfer. For example, real property can only be transferred to a trust by executing a deed. Corporate interests, such as stocks or shares in a small business, may only be transferred with an assignment and the issuance of a new stock certificate from the corporation. If the client owns shares in a co-op, they must go through a formal approval process before their shares can be retitled into their trust.

Because transferring certain assets into the trust can be a hassle or incur additional fees and costs, sometimes clients intentionally keep certain assets outside their trust. A client may opt to forgo the expense and hassle of retitling their residence, presuming that they will one day sell it prior to their death. The client might reasonably conclude that incurring fees and costs to convey an asset into their trust which they intend to sell during their lifetime is unnecessary and wasteful. This is a risky proposition as death or incapacity can occur in an instant, making it difficult or impossible to transfer the property later, undoing the benefits of establishing the trust.

Risks of Leaving Assets Outside the Trust

Some types of assets, such as retirement accounts, must be left outside a trust, but this can also be a trap for the unwary. The

client must always consider the assets that the beneficiary will receive outside their trust as part of their overall estate plan. If a client wishes to change the terms of their trust to provide more or less for their intended beneficiaries, they must be mindful to also update their beneficiary designations accordingly.

Changed circumstances may also require a change in beneficiary designation. The client may have divorced their spouse since naming him or her as the primary beneficiary of their life insurance or retirement assets. Perhaps the intended beneficiary has died, become incapacitated, or is now a spendthrift; failing to update beneficiary designations may expose these assets to creditor claims or disqualify the beneficiary from receiving government benefits.

Safeguards to Prevent Funding Failures

While ideally all assets will be transferred into the revocable trust before death, there are many ways where even well-intentioned individuals will inadvertently fail to transfer assets into their revocable trust. Several safeguards that can be easily implemented to mitigate these risks and ensure that the client's beneficiaries inherit their assets as intended.

When implementing a revocable trust in a client's estate plan, a "pour-over" will should always be executed. A "pour-over" will directs that any assets left outside the trust at the time of death be distributed or "poured over" into the revocable trust. Without a will in place, assets left outside the trust will pass by intestacy.

In addition, clients should consider whether it is appropriate to provide their agents broad powers under a power of attorney to gift their assets, change beneficiary designations, and amend the client's trust, to conform with the client's wishes. These powers help to ensure that additional estate planning can be done at any time during the client's life, even if they become incapacitated.

Lastly, the client should consider naming their trust as the primary or contingent beneficiary of any assets left outside their trust. By doing so, it not only ensures that these assets will ultimately pass to the trust, but it also enables the client to change their estate plan by simply amending the terms of their trust.

Conclusion: Regular Review Ensures an Effective Plan

The reality is that while establishing an estate plan may take as little as a few months, it is not a discrete process; estate planning requires continuous monitoring and occasional updates. Clients should be encouraged to review their estate planning documents at least every four to five years, or at major milestones such as the birth of a new family member, moving to another state, or when there is a significant change in the law, to ensure that their estate plan will function as intended.