The Use of Trusts in Real Estate Transactions

Description

Article by Stephanie Armstrong, Esq.
Senior Underwriting Counsel, First American Title Insurance Company

Introduction

Trusts play a vital role in modern real estate transactions and estate planning. They offer privacy, flexibility, and significant procedural advantagesâ??particularly in avoiding probate and managing complex ownership structures. This article examines the legal foundations of Trusts under Virginia law, their practical uses in real estate transactions, and the critical underwriting and title insurance considerations that title professionals should understand.

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Understanding the Structure of a Trust

Holding real property in a Trust structure creates a legal separation between ownership and benefit. A Trust is a fiduciary arrangement in which one party holds legal title to property for the benefit of another. A Trust has three basic parties:

â?¢ **Settlor (aka Grantor or Trustor):** Creates the Trust and transfers assets into it.
â?¢ **Trustee:** Holds legal title and administers the Trustâ??s terms as a fiduciary for the benefit of others.
â?¢ **Beneficiary:** Person, estate, entity or charitable organization who holds a beneficial interestâ??present or future, vested or contingent.

Note that in the most commonly used type of Trust for holding title to real estate â?? the Revocable Living Trust â?? the same person can have all three roles and serve as the Settlor, the Trustee and the Beneficiary. These roles can also be filled by different people or entities. For example, a Settlor can name a bank as their Trustee and their children as the Beneficiaries. There may also be multiple parties acting as co-trustees or successor trustees if the original trustee resigns, dies or is otherwise not able to act.

A funded **Trust Corpus** is also necessary for the Trust to be valid. The Trust Corpus is all the property owned by the Trust, including real estate, personal property, or intangible assets, plus any income or interest earned. Because the Trust does not exist until the Corpus is funded, you will often see a photocopy of a $10 bill attached to the Trust Agreement as evidence that it is funded.

Why Use a Trust for Real Estate Holdings?

Trusts are increasingly favored in real property transactions for the following reasons:

1. **Privacy** â?? Trust terms remain private and do not become public record (Testamentary Trusts created under a probated will are the exception).

2. **Probate Avoidance** â?? Property held in Trust avoids probate, saving time and expense (again, Testamentary Trusts are the exception).
3. **Estate Tax Planning** â?? Certain Trusts can reduce federal estate tax liability.
4. **Flexibility** â?? Trusts are easier to amend than wills and remain effective during incapacity.
5. **Control** â?? The Settlor can create conditions precedent to a beneficiary receiving Trust assets. The Trust Beneficiary reaching a certain age is a common restriction.

Types of Trusts in Real Estate Practice

Revocable Living Trust â?? The most common type of Trust for real estate, often naming the same person as Settlor, Trustee, and Beneficiary. This is sometimes called an Inter Vivos Trust and it is revocable and amendable by its terms.

Testamentary Trust â?? Created by a probated will, becomes effective only after death, and requires the Trustee to qualify before the Circuit Court Clerk like an executor.

Irrevocable Trust â?? Terms generally cannot be changed; used frequently for charitable planning, life insurance trusts, or tax-driven strategies.

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Sub-Trusts â?? Marital and Family (Credit Shelter) Trusts created under a primary Trust Agreement.

Special Needs Trust â?? Preserves eligibility for public assistance while providing supplemental support.

Business Trust â?? An unincorporated business, trust or association formed under the Virginia Business Trust Act to own and manage property in a business structure. Requires Articles of Trust to be filed. Virginia Code Â§Â§ 13.1-1200 et seq.

Land Trust â?? Not part of the Uniform Trust Code. Virginia Code Â§ 55.1-117 sets forth the parameters for certain trusts to hold real property but this is not commonly used as a method to create a Trust, and most Settlors will still have a signed trust agreement. This statute allows the terms of the Trust to be set forth in the deed of conveyance, allowing the Trustee to act without producing a Trust Agreement.

Note that although a Testamentary Trust is created by a will, the will can name a Living Trust as the Beneficiary of some or all assets of the estate. This type of will is known as a â??pour-overâ?• will because the estate assets are poured into a Living Trust. A Trustee of a Living Trust that receives assets from a pour-over will does not need to qualify before the Circuit Court Clerk because the Trusteeâ??s powers are granted by the separate Trust Agreement.

Trustee Authority and Fiduciary Powers

The Trustee must have explicit authorityâ??either through the Trust Agreement or by reference to a statuteâ??to buy, encumber, lease, sell and convey real property.

A reference in the Trust Agreement to general powers available to trustees in Virginia grants the powers listed in Virginia Uniform Trust Code Â§Â§ 64.2-777 and 64.2-778. It is typical, however, for a Trust Agreement to reference Virginia Code Â§ 64.2-105 (or Code Â§ 64.1-57 if written before 2012) which contains broad powers over real property. Title insurance underwriters will not typically rely on

the general powers for a Trusteeâ??s authority and will look for a reference to Â§ 64.2-105 in the Trust Agreement or power over real property specifically described in the Trust Agreement itself. The Trustee of a Land Trust has the power conferred by the deed itself per Virginia Code Â§ 55.1-117.

The failure of the Trust Agreement or the deed into the Trust to include any powers over real estate is a problem. If the authority of the Trustee over real property is unclear, you should consult with legal counsel or your underwriter before the transaction proceeds.

Transferring Real Estate Into and Out of a Trust

Transfers Into Trust
If the Settlor already owns the property, they can transfer title into their Revocable Living Trust by deed of gift. When the Settlor and Beneficiaries are the same individuals, this transfer may be exempt from recordation tax under Virginia Code Â§58.1-811(12). Trustees may also purchase property in the name of the Trust if authorized by the Trust Agreement.

If a married couple who already holds title in their individual names then transfers title into the name of their joint or individual Trusts, it is important to note whether they originally held title as tenants by the entirety. Virginia Code Â§ 55.1-136 provides that the spouses will retain the protections against separate creditors they had as tenants by the entirety as long as they remain married and the property continues to be held in the Trust or Trusts. This protection is not available if property is purchased directly by the Trust and is not previously held as tenants by the entirety by the spouses as individuals.

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Transfers Out of Trust
Trustees typically convey property using a special warranty deed, which limits warranties to the period of the Trusteeâ??s ownership. This is appropriate given the possible limited knowledge of the Trustee to historical title matters. Some Virginia real estate contracts automatically provide for a special warranty deed when a Trust is the seller.

Virginia Code Â§ 64.2-804 allows us to rely on a Certification of Trust to protect the privacy of the Trust instead of producing the entire Trust Agreement for review for a particular transaction. Many estate planning attorneys will prepare one for the Trustee at the time the Trust is created or amended but most underwriters will require one to be signed as part of settlement as well. It is important to know that even if a Certification of Trust is provided, the underwriter is still entitled to receive copies of excerpts from the Trust Agreement that designate the Trustee and confer upon the Trustee the power to act in the pending transaction.

Assets in a Revocable Trust remain subject to the Settlorâ??s creditors pursuant to Virginia Code Â§ 64.2-747 so it is important to identify the Settlor and run them for judgments and liens when working with a transfer out of a Trust. Remember that there may be protection for individual judgments against one spouse for a married couple who originally held title as tenants by the entirety under Virginia Code Â§ 55.1-136.

Powers of Attorney and Trusts

A Trustee often wants to use a Power of Attorney (POA) in a real estate transaction, but it is generally better to have a co-trustee or successor trustee act instead. Even if the POA allows someone to sign for the Trustee, beneficiaries might still question whether that person has proper authority under the trust. To use a POA in this situation, two things must be true: (1) the POA must clearly permit the attorney-in-

fact to sign for the Trustee, and (2) the Trust Agreement must allow the Trustee to delegate authority and specifically permit the use of a POA. If the Trust or POA does not explicitly allow this, the POA cannot be used. Generally, a Trustee cannot delegate their duties, but if the Trustee is unavailable, the Trust Agreement usually names a Successor Trustee who can take over.

Title Insurance and Post-Policy Transfers

This article would not be complete without mentioning the continuing coverage provided for post-policy transfers into a Trust. Under the 2006 and 2021 ALTA Ownerâ??s Policies, title insurance coverage held by an individual will typically continue when:

1. The grantee is a trustee of a trust created by a written instrument established by the Insured owner for estate planning purposes; **and**
2. The transfer is made without valuable consideration (i.e., by gift deed).

For the enhanced ALTA Homeownerâ??s Policy of Title Insurance, coverage also continues in favor of the trustee or successor trustee of a trust you create for estate planning purposes.

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Conclusion

I hope this article helps you understand the structure and risks involved in insuring Trust transactions. Trusts provide an effective balance of privacy, flexibility, and control in real estate ownership but ensuring valid Trustee authority and understanding statutory requirements are essential to insurable and compliant transactions.

This article is provided for informational purposes only and does not constitute legal advice. The information in this article is general in nature and may not address all issues that could arise in a particular transaction. Parties should consult with their legal counsel for advice specific to their situation.

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Stephanie Armstrong, Esq., is Senior Underwriting Counsel at First American Title Insurance Company and is a former Trust Officer for a national bank. She advises on complex title issues, trust transactions, and fiduciary conveyances throughout Virginia.

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Author
vltaexaminer

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