

Money Unscripted | Wills and trusts: What's the difference?

ALLY DONNELLY: Wills versus trusts, it's one of the biggest questions we get when it comes to estate planning. This is Fidelity's Money Unscripted with Pamela Pirone-Benson, Fidelity VP in Advanced Planning, and me, Ally Donnelly. How do wills and trusts work? What do you need? And why it matters. Pamela, high level, what's the difference between a will and a trust?

PAMELA PIRONE-BENSON: A will is a legal document where you're outlining where you want your assets to go when you pass.

ALLY: And a trust?

PAMELA: A trust is a legal document where you're making either a contract with yourself or somebody else, outlining where you want assets to go. A trust might be circumstance-specific. It really depends on what you're trying to accomplish, what are your goals, what state you live in. So you really need to consult an attorney as to whether or not you need a trust. But there are some fantastic benefits that a trust can bring to you.

ALLY: OK, let's put a pin in trusts for a second and talk wills. You say everyone needs a will. Why?

PAMELA: A common misconception is, oh, I don't need a will. I'm not wealthy enough. Regardless of your age or your wealth, everyone needs a will.

ALLY: How do you get one and what do you put in it?

PAMELA: Generally speaking, you consult with an attorney who's going to help you put together the will. So here are the elements you want to cover in a will. Your executor or personal representative, that's the person that gets the job to settle your estate. Your beneficiaries, that's the person or people that are going to receive your assets.

If you have minor children, you're going to need to think about a guardian. You're also going to need to think about a trustee, somebody who's going to help manage the money under the will.

ALLY: All right. So if I don't have a will, what happens?

PAMELA: Your assets are going to go through the court process. And it's much easier to go through the court process and probate with a will than without a will.

ALLY: Describe the difference.

PAMELA: Well, probate is a legal process where it's just basically more time and money for your family to have to go through after you pass away. If you have a will, that process could be much simpler, but it still means you're going to go through probate. If you don't have a will, the court process could be longer, take more time, and then the court's going to decide where your assets are going to go.

ALLY: So I have a home, I have cars, I have all these things, and I don't have a will, bring me through that.

PAMELA: Sure. So if you don't have a will, your heirs are going to have to apply to the court. It's a probate process. And then the court is going to have a system or an outline of where the assets and who they're going to go to.

And that might not reflect your wishes, right? You may want the car to go to somebody and the house to go to somebody else. So really putting it down in that will be able to get a better handle on where your assets go.

ALLY: So on several of my accounts, it's asking me to name a beneficiary. If I have beneficiaries in place like you just touched on, why do I still need a will?

PAMELA: Well, there's going to be assets you can't put a beneficiary on. In a lot of states, you might own real estate. You can't put a beneficiary. Maybe you own a business, your car. So there's other reasons to have a will-- if you have those minor children. So you can't put a beneficiary on everything.

But the key is that your beneficiaries should coordinate with what you do in your will because your beneficiaries supersede what's in your will, so you want them to match.

ALLY: Meaning, if I've named somebody as a beneficiary on an account, I name Ali. And then in my will, I named Diane. Ali is going to get it but that might not be, in the end, what I had intended. I wanted Diane to have it.

PAMELA: Exactly. So maybe we're avoiding probate by naming Ali. But you wanted Diane to get the asset, so they didn't coordinate.

ALLY: So you want to make sure how you've listed your beneficiaries on an account matches up with how you have things in your will.

PAMELA: Yes, you want to make sure the two are coordinated.

ALLY: Avoid confusion and problems.

PAMELA: Exactly.

ALLY: Got it. OK, that's a will. But bring us back through trusts. Who could have one or who should consider one?

PAMELA: Sure, anyone could have one, but not everybody needs one. So it's really circumstance-specific. But there are some general reasons that people do set up trusts.

ALLY: So give me an example. What are some things people put in trusts?

PAMELA: Often, it starts with the house. You can't generally put a beneficiary on a home in a lot of states. So you can transfer your house into the name of a trust to make that process easier for your loved ones when you pass.

In addition to your home, you can also put your bank accounts, your checking account, your brokerage accounts in the name of the trust as well. I might have a beneficiary that has special needs, and they have health issues and they're not able to manage their own affairs.

I might have houses in multiple states, and I don't want to go through the court system in multiple states. I might have that evil daughter-in-law or son-in-law, and I want to leave those assets to the bloodline. Great reason to use a trust.

ALLY: What are some of the benefits of a trust?

PAMELA: Depending on what type of trust you set up, one is controlling the distribution of your assets when you're gone, avoiding court, avoiding probate. Privacy. A will is public, that's going to be filed in court. A trust may not have to be and can protect your privacy. And in some cases, it might be estate tax savings.

ALLY: All right. Pitfalls?

PAMELA: A trust is generally going to be more expensive to set upfront, so maybe upfront legal costs. There's going to be fiduciaries who are trustees. They're entitled to compensation. Sometimes in different states, there's accountings that need to be filed for the trusts. There may be separate tax returns that have to be filed. And sometimes there may be adverse tax benefits to a trust.

ALLY: So more complicated?

PAMELA: Very complicated. You definitely need to talk to your attorney about whether or not you need a trust.

ALLY: You said there are different types of trusts. Walk me through them.

PAMELA: Let's start with revocable as opposed to irrevocable. A revocable living trust is a contract with yourself. The first part of it says, you're healthy, you're fine. You do what you want. You're the trustee. It has a second section where you're incapacitated. Somebody steps into your shoes. We call that the successor trustee and helps you. And then the third part, if it's going to look like your will. I pass away, this is where I want my assets to go.

ALLY: OK. Give me some examples of revocable.

PAMELA: Sure. You could put your home in a revocable trust-- multiple homes. If you have a second home or a family home, your checking account, your savings account, your brokerage account. In some states, you can even assign your stuff to your revocable living trust.

ALLY: How about the second type, irrevocable?

PAMELA: Irrevocable. Sometimes that's a scary word.

[LAUGHTER]

But an irrevocable trust is set up for a lot of different reasons. Irrevocable is the literal meaning. You put something in it, and you can't change it. That's why it is a little kind of scary at times. An irrevocable trust could be done for a lot of different reasons.

Maybe you want to do gifting and save some estate tax. Maybe you're concerned about a child or a beneficiary getting divorced, or you have grandchildren, or you have certain charities that you care about, and you want to make sure the money goes to those places. You can put those in an irrevocable trust, where you're making those decisions upfront.

ALLY: And they're final.

PAMELA: And they're final.

ALLY: I want you to walk me through the taxes effect with an irrevocable trust.

PAMELA: Often, a technique to get assets out of your estate, to start growing assets estate tax-free is to gift assets into that irrevocable trust. Now, that irrevocable trust becomes like a person. It's going to have to file its own tax return. It's going to have a trustee that's going to control it.

But a simple example-- if you put a million dollars in an irrevocable trust and you die, it's worth \$2 million. You got \$2 million out of your estate. That's not in that estate tax calculation.

ALLY: Interesting. So that's a good way to protect what you have and get as much as possible to your beneficiaries.

PAMELA: Absolutely. If you're looking to do estate planning and tax planning, there's a lot of different kinds of trusts you can use-- some for houses, some for investable assets. So it's a great mechanism to shift some growth out of your estate.

ALLY: What happens with a trust as I'm setting it up? How do I have to do it?

PAMELA: Well, you have this trust and you've outlined your wishes, but your trust doesn't do anything unless you retitle your assets into the trust. You mentioned the home. So after you do a trust, the attorney will help you change the title from the home into the name of the trust-- maybe your bank accounts, your checking account, your savings accounts.

But that is so important to keep in mind, whether it be revocable or irrevocable or trust that springs to life when you're dead, you have to make sure things are titled in the name of the trust.

ALLY: How often do you see it that people don't title it properly or don't fund it properly?

PAMELA: Yeah, I would say that's probably the number one misstep I see in estate plans. You do a great job. You make the decisions. You see the attorney. You outline everything, and then nothing's in the trust.

ALLY: And what happens.

PAMELA: Well, it depends. If it has a beneficiary, it'll go by beneficiary. And if it doesn't have any beneficiary, we're going to go through the will into probate.

ALLY: I want to dig in just a little bit more. So let's take the house example and do it kind of a side by side. So if a house is in my will, what happens? And if a house is in a trust, what happens?

PAMELA: Sure. So if you have a will, and it distributes where your house goes, we're going to go through probate. We're going to have to go to court. That will's going to have to be filed. And there's going to be time and money and some kind of delay.

ALLY: So I'm giving my house to my kids. That's in my will. Figure it out.

PAMELA: Yup, figure it out, go to court, drop off the paperwork, wait a few months, and then we'll have a probate opened, and that executor will be named.

ALLY: So I put the house in a trust.

PAMELA: So if that house is in the revocable living trust, you're going to have a trustee. And that trustee can step into your shoes without having to go to court to be named because you already named them in that trust.

ALLY: For both wills and trusts, how often should you revisit them?

PAMELA: Well, there could be a life event, a change sometimes. I recently had a client. Her trustee passed away, so she needed to make a change on her trust. Name a new trustee. At a minimum, I would say every three to five years, she should take a look.

Now, to just go back to irrevocable for a minute, those should be reviewed every year with your accountant and an attorney. Laws change, tax laws change, and there's a lot of ongoing maintenance with irrevocable trusts.

Also, let's say you have a house in one state and you're going to buy that vacation home you always wanted in the second state, we don't want to go through the court system in two states, your family or your friends, when they pass away. That trust can help avoid the multiple probates.

ALLY: Give me your final thoughts. As people are walking away from this conversation, what do you hope really hits home?

PAMELA: Well, that everybody should have a will, regardless of your net worth or your stage in life. As it comes to a trust, you may or may not need one. It's something to consider and to think about. You want to consult with your attorney. But really important, if you're going to do that trust, make sure your assets are titled properly to reflect your wishes and what you put down in that trust.

ALLY: Excellent. Pamela, thank you.

PAMELA: Thank you so much for having me, Ally.

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