CHAPTER SIX

Trustees

A trustee is someone you can trust—someone who will take charge of your trust documents after your death and carry out your wishes. This person (or people) is typically one or more of your adult heirs or members of your family.

What does a trustee typically do? The trustee takes care of not only the financial things such as gathering together investments, insurance death benefits, and selling real estate but also the more mundane things like cleaning out the garage and basement, making funeral arrangements, doing your final income tax returns, and paying any leftover bills. So while it does take some time, most of these duties do not require the services of a lawyer. Following the instructions in this book will make the job quite easy for most trustees.

How can you be sure your trustee can be trusted? There are ways to be more certain your trustee will do the job faithfully and honestly. One good way is to name two trustees as cotrustees to act together, especially if it is a blended family in which each parent has a separate set of children. Taking one child from each side of the family creates a situation where they watch each other and are more likely to do things properly.

In situations where there are no trustworthy people with whom you are comfortable, you can name a bank trust department or, as a last resort, have a provision put in your trust that the trust is to be registered with the probate court for supervision. (The name of the court handling probate cases is

different in some states. It may also be called a circuit court, superior court, or district court, but it is the court that handles the estates of deceased people.) Or, even better, have a provision in your trust to have the court appoint a trustee while "acting in a ministerial capacity" rather than assuming full control and supervision of the trust. Trust supervision by the court is something akin to probate and is to be avoided if possible.

The law calls a trustee a "fiduciary" and, as such, imposes on the trustee certain legal obligations. A trustee is bound by the terms of the trust but also by the state law governing fiduciaries.

For example, there is in most states a set of laws commonly known as the "Prudent Investor Rules." These basically say that a trustee must be conservative and careful in managing the assets of the trust. The trustee must not put the trust assets in jeopardy by making risky investments. The trustee has statutory obligations to keep good accounting records and keep the trust beneficiaries informed as to what is happening with the trust. You need an organized trustee who keeps good records, so it is very important to choose the correct trustee.

Years ago, it was common to choose professional trustees—usually the trust department of a local bank. That still happens, but typically for larger trusts. The problem with professional trustees, in my experience, is that they are not too willing to exercise their discretionary power to make distributions to beneficiaries.

As an example, I was contacted by a twenty-one-year-old college student who was the beneficiary of the trust of her deceased grandfather. The bank was the trustee, and the trust said that the beneficiary was entitled to use the money for "educational purposes" and any other expense that the bank thought appropriate. There was about $1.5 million in the trust account.

The student had requested money to buy a used car because she wanted to live off-campus in an area with no bus service. The bank refused to give her anything for a car, saying that was an inappropriate and noneducational expense. Had her parents been the trustees instead of the bank, she probably would have gotten the money since it was not, in my view, unreasonable.

Most people choose family members as trustees to simplify things and keep the costs down.

YOU (AND/OR YOUR SPOUSE) AS TRUSTEE

The trustee is the one who is in charge of the trust. In most cases, the grantor

(the maker and owner of the trust) is his own trustee during his lifetime. Couples usually have joint trusts or are cotrustees. If one of the couple dies, the survivor usually remains the sole trustee until death or disability. But not necessarily—it depends upon circumstances. Sometimes in situations where each spouse has his or her own trust, the directions are to name the survivor plus one of the decedent's children as cotrustees. Every situation is different, which is why there is no one-size-fits-all trust.

After both grantors die or are incapable of acting as trustees, the "successor trustee(s)" takes over as trustee. The successor trustee is not a grantor and cannot change the terms of the trust in most cases but can only carry out the terms of the trust put in place by the grantor (though there are special situations where trust provisions can be changed by a court or a "trust protector," described later).

The trust becomes irrevocable (unchangeable) after the death or disability of the grantors but is revocable (changeable) during their lifetimes so long as they are capable and competent. These are the general rules. However, people often have reasons to do things differently.

For example, one of the two grantors may be the financial manager and the other grantor may not be capable of handling the business decision-making that a trustee needs to be able to do. In that case, the trust may provide that at the death of the financially capable grantor, another person will act as either sole trustee for the surviving grantor or as a cotrustee with the survivor.

Sometimes a couple wants to be certain that a survivor will not be tempted to misuse the trust assets in such a way as to thwart the intentions of the first grantor to die. In that case, a cotrustee may be named along with the survivor just to be certain that trust transactions are being done properly and honestly according to the terms both grantors set up when alive. This method unfortunately can cause friction between the survivor and the cotrustee, because the survivor is no longer solely in charge of her financial affairs. But it is a pretty much guaranteed way of assuring that the trust rules are followed since all trust transactions require two signatures.

Bank trustees typically charge 1 to 1.5 percent of the trust assets annually as a fee for serving as trustee. Family members who are also beneficiaries usually do it for free; however, it is not uncommon to specify a payment to a trustee for carrying out your trust instructions. Trustees are, of course, entitled to any actual expenses they incur, but also may have to take time off work to meet with accountants or real estate agents or to do other trust-related

business. Allotting a set amount of money as a trustee fee on top of whatever the trustee may inherit is not at all unusual and is, I think, appropriate. The amount will depend, of course, on the level of work involved. If the trustee is merely going to wrap up your estate, pay the bills, and hand out the money, a lump-sum trustee fee appropriate to the size of the estate would be determined.

However, if the trustee is to continue to act as trustee in years to come to care for the trust fund of a minor or disabled person, an annual fee should be allocated. Keep in mind that a trustee fee is taxable income to the trustee, whereas if you left the trustee a share of the trust as an heir, it would not be considered income, so a share of the estate is more valuable than an equivalent amount of money as a fee. The trust language can make it clear that the larger share is a gift made in gratitude to the person acting as trustee, and not as payment for services.

BACKUP TRUSTEES

What if your selected trustee cannot or will not act as trustee when the time comes? It is always a good idea to have a second and even a third alternate trustee named in your documents.

Just because you have named someone to be your trustee or executor does not mean they are obligated to do it. A few years ago, a woman came to me to represent the estate of her neighbor. The woman had been named by the neighbor as the executor of the will. The estate was not large and the deceased had several children in other states, none of whom liked her. After discussing the probate process with her, I could see she was not happy with the prospect of the big job ahead of her. Finally, I told her she did not have to do it.

She was surprised, having assumed that she had no choice. “Let one of the children be the executor.” I said. The will had no backup named, so the children would either have to agree on one or have the judge appoint someone. She left the papers with me and very cheerfully said she would call one of the sons to tell him her decision.

In your trust, there should be language that provides a mechanism for choosing an alternative trustee if there is none named who is able to do the job. I suggest allowing the beneficiaries to elect a trustee if you can’t come up with one, with the guardians of child beneficiaries voting for them. There may be other requirements if the trustee will be enforcing restrictions on

when and how a beneficiary receives his share of the trust. You cannot have a trustee in charge of his own restrictions, especially in a special-needs trust situation.

WHO CANNOT BE A TRUSTEE

A special-needs trust is a trust set up for a person who is disabled in some way and who relies upon need-based government programs for his support and/or medical care. Qualifying for Medicaid for example, may be extremely important—even vital—to a person with certain needs. Expensive drugs and medical treatment may be far more important to a person than an inheritance, and inheriting something may disqualify that person from those benefits. The reason is that in most cases, a person can only own a certain maximum amount of assets to qualify for the benefits. If he has the ability to control the assets in the trust, the government might say he has the ability to give them all to himself, thereby putting him over the threshold for disqualification. So a discretionary trust is often created to allow a trustee to give the beneficiary certain things to enrich his life but not enough at one time to affect his benefit programs.

Therefore, the beneficiary of a special-needs trust cannot be the sole trustee of that trust. In a special-needs trust, the trustee has the discretionary authority to make whatever distributions the trustee deems appropriate for the beneficiary, provided that benefit programs are not reduced by the distribution. A special-needs beneficiary may end up being disqualified because of the assumed ability to exercise trustee discretion in favor of the beneficiary.

A trustee must be of legal age, must be mentally competent, should be a resident of the United States, and must not be a ward of the state under a guardianship order. It helps if the chosen trustee has a good business head and is well organized. Check with your attorney to see if there are special restrictions in your state. A bond is not normally necessary, but if it is, the trustee has to qualify for the bond. It would usually be required only in a court-ordered guardianship/conservatorship situation.

A bond is a type of insurance policy that covers any losses to the estate due to the misfeasance or malfeasance of the person bonded. Bonds are only given to bondable people—that is, those who have no criminal history or past conduct that would make them a possible risk to the insurance company. So if the conservator of a person’s money runs off with it, the bonding company

makes good the loss, then goes after the conservator.

COTRUSTEES

I usually recommend cotrustees if possible. The reason is that two or three people acting together are less likely to procrastinate in carrying out the trust instructions and are going to be more likely to keep good records and follow the trust instructions. They watch each other. A trust, being nonsupervised by a court, has no one to report to and no real enforcement mechanism to control the trustee except after the fact. Cotrustees minimize this potential problem.

Here's an example: one of four children is named as trustee. He is supposed to gather all the assets together, pay the bills, sell the real estate, and divide the remaining assets among the four of them. But he is incompetent or, even worse, crooked. So he doesn't tell everyone what he's doing, spends much of the money on himself, and sells things to his friends for less than value, and when he finally pays off the other three, it is only a fraction of what they should have gotten. Okay, he wasn't trustworthy and shouldn't have been named as trustee. What can the others do? They can petition the court to make him account for the missing assets, but if it's gone and he doesn't have anything left, there is no real way to get back what has been wasted. Cotrustees would have avoided that situation.