SELECTING YOUR PERSONAL TRUSTEE

A decision fraught with pitfalls and potential missteps

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The selection of a trustee for one's personal trust is arguably as important as the provisions of the trust itself; it should not be an afterthought, considered to be inconsequential. We will discuss many of the factors one should consider in the selection process.

The authors have worked together for a number of years for traditional "corporate" trustees, and most recently with a directed trust company with a modern business model.   They have worked in the personal trust industry for a combined 75 years, plus or minus, and have seen a great many changes in the profession they have chosen for their careers.

But while the way in which trusts are being used today, (for example, the great change in the taxation of estates, and the evolution toward the "tri-furcation" of trustees' responsibilities, the Dynasty Trust with no rule against perpetuities, the use of decanting to effectively change the provisions of a trust, and the evolution of the role of the Trust Protector) one of the things that has **not** changed is the necessity of identifying the right trustee for one's personal trust.

We will start by considering the various functions that a trustee of a personal trust may be required to perform. Then we will look at the choices of trustees available today, with our assessment of the strengths and weaknesses of each type of trustee.

First, though, it would be helpful for the uninitiated to define the term "personal trust".

At its simplest, a trust is a set of instructions (normally written) telling the trustee what to do with the trust assets (sometimes called the trust corpus, or body) for the benefit of the beneficiaries (usually defined as current beneficiaries and remainder beneficiaries – those remaining after the grantor or initial beneficiaries are deceased.)

FUNCTIONS A PERSONAL TRUSTEE MAY PERFORM

The basic functions required of most trustees are:

- Provide for safekeeping the trust assets such as bank accounts and brokerage accounts, as well as virtual holdings such as hedge funds, derivatives and LLC interests
- Accounting to current and remainder beneficiaries regarding trust assets, investments and transaction activity on a timely and periodic basis
- Overseeing the management of the trust's investments, except where the investment function is "directed" to a directed investment advisor
- Ensuring that trust tax reporting is completed in a timely manner, either in-house or outsourced to a competent firm, as well as ensuring the tax information is provided to the grantor and/or beneficiaries
- Making required distributions as defined in the trust's terms

- Making discretionary decisions regarding the distribution of income and/or principal of the trust, in accordance with the terms of the trust

An effective trustee will have many years of experience administering trusts. They will work with both those establishing trusts (grantors) and those who benefit from the trusts (beneficiaries). A professional trustee typically will have 7 to 10 years of experience to be qualified to competently administer a trust.

The expertise that a professional trustee absorbs over those years crosses many fields, including:

- The entirety of trust law, including statutes, regulations, private letter rulings and case law
- Financial planning, including budgeting and managing the trust's cash flow
- Trust accounting, which typically includes the separate accounting for the beneficiaries who receive current income and those who have an interest in the principal upon the death of current income beneficiaries
- Real estate transactions and management, both of residential properties that a trust might hold, as well as commercial properties
- An understanding of business, especially closely-held or family businesses, which could vary from farms, vineyards and agricultural holdings, to a pharmaceutical company or a hotel. A trust may hold such assets, and the trustee must be qualified to make sound decisions in the on-going administration and eventual disposition of such assets

- State and federal income and estate taxes specifically, as those relate to the highly complex taxation of trusts
- Investments, including traditional stocks and bonds, oil and gas interests, hedge funds, commodities, mutual funds, exchange traded funds, and other miscellaneous assets
- An understanding of psychology, and especially dealing with family interactions and conflicts. Many trustees have been trained in facilitating family meetings and counseling multiple generations of a wealthy family, ensuring the continuity of the family's wealth, and often more importantly, the legacy left by the founder of the wealth
- A broad knowledge of charitable planning and wealth preservation, including helping wealthy families teach younger generations how to preserve wealth and use it for worthwhile purposes. A good trustee will help families to develop human, social and intellectual capital as well as merely preserving wealth

TYPES OF PERSONAL TRUSTEES

There are a number of options available in the selection of a trustee to carry out the duties and responsibilities of a personal trust. Those options fall into the category of **Corporate Trustees** and **Individual Trustees**.

CORPORATE TRUSTEES

One common feature that is considered an advantage by most corporate trustees is that a corporation doesn't die. It lives forever, and while individual employees may come and go in the role of trust officer, the entity will exist indefinitely. This can remove some uncertainty as to the consistent administration of a trust compared to naming an individual trustee.

Other advantages of corporate trustees include having trust accounting systems for reporting and tracking income and principal account activity, policies and procedures that are acceptable to state and federal bank regulators, and they conduct internal audits and examinations periodically to ensure they are carrying out their fiduciary responsibilities properly and documenting fiduciary activity.

TYPES OF CORPORATE TRUSTEES

- Large, national money center banks
- Regional bank
- Community banks
- Independent trust companies

There are several different kinds of corporate trustees. The most traditional are the **large, national money-center banks**, such as JP Morgan, Citibank, Wells Fargo, and Bank of America. We will also include in this category the large, multi-family office institutions, such as Bessemer Trust.

Some trust beneficiaries find that corporate trustees can be inflexible and bureaucratic, having to go through committees that can delay discretionary or investment decisions. They can also be slow to respond to inquiries from beneficiaries and other interested parties. There can sometimes be a high level of trust officer turnover, such that a trust could have many different trust officers over the duration of the trust.

Because large banks are often more bottom-line-driven and have higher overhead, their fees are often much higher than regional or community banks, and much more costly than individual trustees' fees. They typically have higher minimum fees, essentially eliminating much of the trust market. Some have minimum trust asset market value requirements as high as $25 million. Most will not accept a trust unless it is at least $2 million in total market value.

A large institution will often be willing to take on more complex trust administration than small banks, independent trust companies, and individual trustees. Offsetting this is their frequent unwillingness to take one-off trusts that are not associated with a large family relationship such as Irrevocable Life Insurance Trusts (ILITs) and Supplemental Needs Trusts (SNTs) for special needs beneficiaries.

Smaller, **regional banks,** such as SunTrust and BB&T**,** work much like the large, money center banks, so we will not differentiate them, except that their fees might be slightly lower.

However, **community banks** can differ significantly from the larger banks, being local, and frequently have lower fees than the larger banks.

Independent trust companies are another option in the Corporate Trustee category. They differ widely, and many have unique business models that may be attractive. For example, some independent trust companies specialize is Special Needs Trusts, some in self-directed IRAs, and others in highly complex trust administration. They may also have very limited investment options, including outsourcing their investment capabilities to a third party manager, using an ETF-only investment option, or in some cases, will serve only as a directed trustee, with no investment management capability. Fee methodology (that is, flat fee or asset-based fee) and minimums can vary widely, so it is best to shop carefully.

INDIVIDUAL TRUSTEES

- Family Members
- Family Advisor
- Professional Individual Trustee

Family member – a family member is frequently named as trustee, simply because there seems to be no other logical choice. The advantage to having a family member serve as trustee is their knowledge of the family dynamics and values.

Family members have the benefit of knowing the family, but are generally not a good option, as they often have limited time to carry out trustee responsibilities and do not have the necessary experience, resources or systems to fulfill the duties of a trustee. They can be challenged with a multitude of conflicts that may preclude the ability to make sound, unbiased discretionary decisions. Family trustees may not understand trust reporting requirements. Examples of family members not performing adequately in their capacity as trustee are failure to report to the beneficiaries the trust's assets, investment strategy or the terms of the trust that detail the income or principal to which the beneficiary may be entitled. Such situations drive families apart and frequently result in litigation. Fiduciary litigation attorneys tell us that the majority of fiduciary lawsuits are against family member trustees, and not corporate trustees.

Family advisors are individuals who are also available to families who do not wish to name a family member as trustee.

- Financial advisors may serve as individual trustees but they may not have the requisite experience. Many financial advisory firms' compliance departments do not allow them to accept trustee appointments.

- Attorneys and CPAs sometimes accept individual trustee appointments and can handle simple trust administration, but typically are not well suited to the more complex aspects of trust administration, such as working with grantors and beneficiaries or managing closely held businesses owned by trusts. They seldom have an experienced trust officer on their staff to provide the client service expected by grantors and beneficiaries.

Professional individual trustee – a somewhat newer and less obvious choice, a number of trust professionals from the banking world have established themselves as professional, independent, individual trustees, filling a big gap between large and small institutional trustees and family members.

A professional individual trustee's primary responsibility is trust administration. They are typically individuals who have years of experience working in the trust industry and understand fiduciary duties and they have the independence and ability to be unbiased. An experienced individual trustee provides the benefits of an experienced corporate trustee without burdensome bureaucracy and high fees.

It is important to choose a professional individual trustee that has the willingness and ability to handle complex trust administration when necessary. If the individual trustee you choose has the capabilities to administer the trust, they are likely to be responsive, stable and the least expensive trustee solution.

CONCLUSION

There is a broad range of possibilities in the selection of a trustee, and the decision has enormous consequences for the beneficiaries and in carrying out the intent of the grantor.

So often over the years we've heard grantors select a trustee based upon where they have their checking account, or choose in a family member because no other options were discussed.

We've shown that potential trustees have a wide range of capabilities, regulation, sensitivity, experience, systems and business models. It is incumbent upon those advising clients, and the trust creators themselves, to evaluate all of the options and to select a trustee based upon the best long-term interest of the trust and the beneficiaries.

Authors:

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