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PERSONAL TRUSTEE ROLES

“Tri-furcation” is the new norm

by

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A personal trust is simply a set of instructions telling the trustee what to do with the assets of the trust for the beneficiaries of the trust.

Trustees of personal trusts (as opposed to ERISA trusts or corporate trusts) can be individuals (such as family members, an attorney or other trusted advisor), or a corporate trustee, (such as a trust department of a bank) or an independent, non-depository trust company, (granted trust powers by either the federal government or a state).

Such trustees, of whichever type, have traditionally performed three types of functions:

- Overseeing various administrative functions of the trust, such as custody of the trust assets, record-keeping, tax reporting, reporting to the beneficiary or beneficiaries, and making required distributions of income or principal,
- Managing the trust assets in accordance with the provisions of the trust, whether liquid assets such as cash, stocks and bonds, real estate, a closely-

- held business interest or other tangible or intangible assets,
- Making discretionary decisions in accordance with the trust instrument, which may include discretion over the income and principal of the trust to living beneficiaries, including the grantor of the trust, and/or other specified living beneficiaries of the trust.

Then, in 1986, the State of Delaware passed a statute formalizing the ability of the trust instrument to “direct” the trustee’s actions, or to appoint a “directed trustee”. Initially, this led to the concept of “bi-furcating” a trustee’s actions by separating just the investment function from the other functions.

There are many reasons why this became a popular option for people creating trusts, and is the topic of another of my articles. In short, however,

- disillusionment with corporate trustees’ investment performance (whether deserved or not),
- the excessive use of the bank’ common trust funds or its own proprietary mutual funds,
- the transparency provided by the internet as a resource for selecting investment management solutions,
- increased use of independent, non-bank investment advisors by wealthy families, and
- ever increasing fees charged by bank trustees

all led to the increasingly popular option of using a family's existing investment advisors rather than the "big bank" trustee to manage the trust's investments.

A number of other states, including South Dakota and Nevada, and including now more than 18 states, such as New Hampshire and most recently Tennessee, have "directed trust" statutes, along with other modern trust concepts, such as the right to "decant" a trust, and the formalization of the role of the "Trust Protector".

As more and more trusts and estates attorneys became familiar with such options, the more frequently creators of trusts choose to establish trusts using the statutes of such "trust-friendly" states, and this has led to the rise of a whole generation of new trust companies capitalizing on those states' statutes.

At a recent estate planning conference of the Heckerling Law School in Orlando, the number of trust company exhibitors tells the whole story. The traditional trust companies represented a small portion of the total, and the newer trust companies, from the states of Delaware, South Dakota, Nevada, New Hampshire and Tennessee, represented the majority. Many of the latter do not manage investments, but serve exclusively as a "directed" trustee, for a significantly lower fee.

The business model of these trust companies is to provide trust administration but no investment function, leaving that to the "directed trustee" or "direction advisor".

That leads us to the evolution of the next concept, which I call “tri-furcation” of the trustee’s functions, or elimination of the discretionary distribution decisions from the administrative trustee’s responsibilities.

Today, we see this tri-furcation in many trusts where the grantor, on the advice of the drafting attorney, is seeking the lowest possible cost of having a good trust jurisdiction. This has been exacerbated by the a growing compression of trustees’ fees. For example, some corporate trustees now charge less than \$2,000 per year to serve as a directed trustee, with a small supplemental charge if they are given responsibility for making discretionary distributions.

Essentially, many clients creating trusts today are seeking the lowest possible cost of creating and administering a trust, by selecting a corporate trustee in a trust-friendly state, but having that trustee perform only the minimal administrative functions, and appointing a directed investment advisor and a directed distributions advisor.

I will delve into the pros and cons of such selections in another paper, but trustee tri-furcation is here to stay, and the day of the traditional, big bank trustee, assuming all of the functions of a trustee, are numbered.

Richard Trumpler is a 46 year veteran of the trust industry, known primarily for his 30 year track record of taking over 5 distressed trust company operations and making them compliant and profitable. In his most recent capacity as Chief Operating Officer of a privately owned trust company in New York City, he successfully implemented a Private Label Trust offering, with clients including Family Offices, Law Firms, a commercial bank and Investment Advisory firms.

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