

# BEING A TRUSTEE

## WHAT IS A LIVING TRUST?

The Living Trust is a legal entity into which property transferred by you, either during life or at death, for your benefit and the benefit of your spouse, if you are married, or for the benefit of another, if you are not.

The two major reasons why individuals use a Living Trust are to appoint a competent successor trustee that helps in avoiding a conservatorship and to avoid probate.

In discussing a Living Trust we have 3 major roles you as creator of the trust can play. The person who creates the trust is sometimes called the “grantor” or “settlor” or “trustor.” The person who manages the trust assets is called the Trustee and the person who receives the benefit of the trust is called the beneficiary.

### The Trustee – A Fiduciary

In the beginning you are the “Trustee,” the person(s) in charge of managing and controlling the property inside the trust. The Trustee holds legal title to the property in trust for the benefit of the grantor or other beneficiaries of the trust. While you are capable and alive, you can be the Settlor, Trustee and Beneficiary of your own trust.

If you ever decide to let someone else take over, you need to make sure that you have a successor trustee listed in your trust document or you have the “power to appoint” a successor trustee which can be a friend (ill advised), family member (lots of pros and cons), private professional fiduciary or corporate fiduciary.

**We believe that the naming of a successor trustee is one of the most important decisions you will make in planning your estate.** It will determine who takes care of you if and when you need help because of dementia, ageing or injury. Your Successor Trustee will decide who will be your care giver, determine type and frequency of medical care, will you live at home or in a board and care, etc. Trustees make decisions that affect your daily quality of life and this is in addition to managing your assets.

Managing property or assets is the easiest part of being a trustee although most individuals are not comfortable in managing assets that are not their own. Managing the expectation of the beneficiaries and the family relationships is trustee’s most difficult role. Just because you have named a trustee in your document does not mean they will accept the role of being your trustee at the time it is needed.

Over the centuries, rules have developed which impose duties on persons acting as trustees for another person. In 1986, the California legislature enacted statutes which list many of those duties. The

Trustee of any trust is said to be in a “**fiduciary relationship**” to the Beneficiary, under which a high standard of conduct is required of the Trustee in administering the property for the benefit of the Beneficiary.

Trustees should be particularly aware of the following fiduciary duties:

**Duty to administer trust:** Trustee must follow the instructions in the trust document and are not free to administer the assets in some other manner.

**Duty of Loyalty:** Trustee cannot use the trust assets for his or her own benefit.

**Duty to deal impartially with beneficiaries:** A trustee cannot favor one beneficiary over another and this becomes critical when the trustee is also a beneficiary.

**Duty to take control of and preserve trust property:** The successor trustee needs to place the bank and brokerage accounts, etc. under his or her control and invest the assets wisely.

**Duty to account to Beneficiaries:** The trustee provides detailed statements regarding all the financial transactions of the trust. Think of it like a bank statements that reports a beginning balance and an ending balance and all transactions in between.

When the successor trustee takes on the role as trustee the trustee must contact all your financial institutions, property records, utility companies, etc. informing them of a change in status of the trust.

The Beneficiary is usually an individual who is entitled to receive income and/or principal from the trust and perhaps enjoy the use of certain trust assets; for example, the right to live in a family residence during the administration of the trust. There may be one or more persons entitled to trust income and/or principal at the same time.

If you are acting as Trustee for your own trust, or perhaps for yourself and your spouse, it is still important that you keep the trust’s property separate from your other property and follow the rules with regard to proper record keeping and prudent investment of trust assets so that in the event of your incapacity or death, your successor Trustees will be willing to assume and continue the Trusteeship without too much effort and locate assets. Your trust has a provision that indemnifies (absolves) the successor Trustee from any wrongdoing by you or another predecessor Trustee, which should alleviate most of the concerns of the successor Trustee. Yet it will be much easier to administer your estate trust once you’re gone if you take the time now and in the future to document your activities within the trust.

As previously mentioned, the creation of a Living Trust occurs during your lifetime. To avoid probate, as Settlor you must transfer property to the trust. If you forget something or fail to transfer the property to the trust during your life, the pour-over will is available to transfer the property that is subject to probate to your trust. However, this is a more expensive way to transfer the property than by doing it yourself.

The Beneficiary is the person for whom the Trust is being administered that is, during your life it is you who will receive the benefits of the trust. When you die, the trust may call for distribution of the remaining assets outright or to be held in trust for certain individuals. These persons are called the “remaindermen.” They receive the “remainder,” or what is left of the trust, when the trust terminates.

You, as trustee of your own trust, do not need to worry about the rights of the remainderman. If you are married, and your spouse is the successor trustee of any trust established for your property at your death, the surviving spouse will owe a duty to the remainderman over that trust.

In many trusts that are created for husbands and wives, two or maybe three trusts are created at the death of a spouse. Some of the trusts, namely the survivor’s trust and the marital trust, are trusts that are for the primary benefit of the survivor, and the remainderman’s interest is secondary.

In the exemption or bypass trust, however, although the surviving spouse may be given certain rights during life, the survivor as Trustee should be aware of the remainderman’s interest and try and preserve the trust estate for them. At this point, the surviving spouse trustee becomes a fiduciary.

### **THIS IS COMPLICATED: WHERE DOES A TRUSTEE START?**

#### **1. Review the Trust Document**

For you as Trustee of your own Trust, you will not notice a difference in how you have changed title to your assets. The assets within the trust will be just as available to you as before, as if you did nothing different.

At the death of a spouse, or if you are administering the trust for another person, you will see a big change in the way things are done. This is where the work begins.

A Successor Trustee is not the owner of the property and as such needs to study the Living Trust which outlines Trustee duties and authorities. The Trustee will pay particular attention to the provisions dealing with the distributions of income and principal. Next, with the Trustee’s powers and the administrative provisions; many of these powers or administrative provisions will not be applicable. However, they are designed to cover a multitude of situations which might arise; and, in such event, they would become important.

Again, the powers are typical powers that you as an individual have but never think about. Of course, you have a right to borrow, loan, invest, sell, etc. But unless these powers are written in the trust document the Successor Trustee would not have those same powers over the assets held in trust. Therefore, even though the trust powers seem extremely broad, you will want to maintain the same flexibility you now have over your assets after the assets are transferred in trust. While you are the Trustee of your trust, you can virtually do anything you want. When the

Successor Trustee takes over at your incapacity or death, the burden of acting is no longer so easy; the Trustee must do what is best for the beneficiaries, following the “prudent investor” rules, or the Trustee can be surcharged (sued and be liable) for the Trustee’s mistakes.

## **2. Checking Account**

One of the first steps in setting up the trust is transferring your personal accounts to a trust checking account. Go to your bank and have them change the name on the account from your name as an individual, or husband and wife, to you as Trustee of your trust. It is as simple as changing the name. Resist the bank representative who wants to establish a new account for the trust. It is not necessary and will only add more cost. Some, but not all banks, ask to see a copy of the Living Trust before opening the account.

If you don’t serve as your own Trustee the checking account should be in the name of the individual serving as Trustee, as follows: “JOHN DOE, Trustee,” followed by the Trustee’s address. This generally is adequate. Some Trustees go further, however, and have the checks printed: JOHN DOE, Trustee U/LIT MARY SMITH, DTD 7/10/9X. This signifies that John Doe is the Trustee under a Living Trust dated July 10, 1 99X. Some institutions will want to use their own abbreviations. However, you don’t have to label yourself as Trustee on your checks, unless you have a desire to do so to keep the account separate from some other account you may have.

The Successor Trustee follows the same steps with the financial institution showing the bank the original Trustee death certificate and driver’s license showing they are the person named in the Trust document.

As professional fiduciaries we use the checking account to record all in and out trust cash transactions, to show when funds are received or disbursed. This ensures a trail for anyone else to review.

## **3. Principal Office of the Trustee**

Generally, the Trustee’s business or residence address should be used as the official address of the Trust. When the Successor trustee steps in a change of address notice should be one of the first duties.

## **4. Trust Identification Number**

As a settlor, if you are the Trustee of your own trust, you are not required, or for that matter allowed anymore, to obtain a separate taxpayer identification number for your trust.

However, when you die, your Successor Trustee, under the Internal Revenue Code, the trust, becomes a separate individual for tax purposes; and, as a result, the trust must have a separate taxpayer identification number (a social security number of sorts). Upon receipt of the number,

the Successor Trustee informs all financial institutions in which the trust has an account, as well as the disbursing agents for all corporations in which the trust holds stock, of the identification number. They will need this for income tax purposes and will furnish the customary Treasury Form 1099 at the end of the year confirming income paid to the trust.

## **5. Trust Income Tax Returns**

Again, as a settlor, the trust is not considered a separate tax entity and is not required to file a separate tax return. All income from the trust is reported on your Form 1040 like any other income you receive.

However, a Successor Trustee is required to file California and Federal Fiduciary Income Tax Returns for the trust each year. While the trust is revocable, the income reported by the trust is not taxed to the trust but to the income beneficiary. When the trust becomes irrevocable, the way in which the trust is taxed will depend on the type of trust you have (“simple” or “complex”) and on how monies are distributed.

## **6. Trust Records**

A Successor Trustee must establish a bookkeeping record for the assets of the trust, in addition to the trust checking account. In this record, we would keep a running list of securities and real property, showing their “cost basis” for income tax purposes in the event of future disposition. Also, we would prepare an annual inventory of all trust assets and an accounting to the beneficiaries.

## **7. Selection of an Accountant**

A Successor Trustee should carefully consider retaining a knowledgeable accountant to assist in the preparation of trust income tax reports and to give advice with regard to setting up whatever records of account may be necessary.

## **8. Cost Basis of Assets**

Consider documenting the cost basis of the various assets being transferred to the trust. Capital gain or loss will be determined by the difference between the selling price and the cost basis of such assets as securities and real estate.

## **9. Insurance Review**

If real property or an automobile is a trust asset, the Settlor and Trustee should consult the Settlor’s insurance agent to have casualty (fire, etc.) and liability policies endorsed to include and protect both Settlor and Trustee.

## **MISCELLANOUS ADMINISTRATIVE ISSUES**

### **Distribution of Income and Principal -Budgeting**

The Successor Trustee should examine the Living Trust to determine whether the income is to be accumulated and added to principal, forming a common fund, from which payments can be made to the Settlor as requested; or, whether the income is to be paid to the Settlor as received, and principal invaded only upon request or in the event of necessity.

### **Trustee's Compensation**

A Successor Trustee, if a family member usually elect to serve without a fee, although as Trustee they are entitled to reasonable compensation for services (i.e. between 0.5 % and 2% of the value of the trust assets, depending on the complexity of administering the trust estate).

We encourage family members who serve as a Successor Trustee to take a fee since the work is burdensome and usually underappreciated by the other beneficiaries.

A Private Professional Fiduciary and Corporate Trustee should always provide a fee schedule and fees range from one to two percent of the assets in the trust per year.

### **Separation of Community Property and Separate Property of Spouses**

When a trust contains more than one type of property (for example, community property and separate property), the assets in each classification should be segregated.

When a trust is established by an unmarried person, the trust property, of course, is his or her separate property.

In the case of married couples, however, trusts are often established for the administration of the separate property of either spouse, or for the administration of their community property. If the trust is established by either the Husband or Wife for the administration of his or her separate property alone, no segregation for tax, accounting and administration purposes is necessary. The same is true if all the trust assets are the community property of the spouses.

However, as in the case of most trusts of this kind, when a trust is established which includes not only community property of the spouses but also some separate property of either or both the Husband and Wife, the trust instrument itself provides instructions for the distribution of income and principal from each of these three categories during the lifetime of both spouses and also provides instructions as to the division of the trust estates into separate trusts upon the death of either spouse.

## **Value added Resource**

For any Estate Planning, Trust Administration, Trust review, Third party professionals; questions or concerns, feel free to contact me via email or phone.

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