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Choosing your trustee

More and more affluent families are turning to trust-based solutions for their wealth management and inheritance problems. However, a trust is only as good as its trustee. Have you been asked to serve as trustee, perhaps for a parent's trust? Do you plan to ask your child to be your trustee? Although such a course of action may be a natural impulse, it may not be the best approach.

A family member has the advantage of personal understanding of the trust beneficiaries, and that is no small thing. Unfortunately, family members usually lack experience and ability in several other crucial areas.

Amateur trustees—watch out for these traps

There are many ways for a trustee to fail to meet the obligations of sound trust management.

Faulty records. There's much more to trust accounting than balancing checking accounts and keeping track of portfolio statements. Income, asset values and distributions must be reported to the beneficiaries on a regular basis. "Beneficiaries" refers not only to those who receive current trust income, but also to those who will receive the assets when the trust terminates. We suggest a team approach, including a trust attorney, a tax professional and an investment manager. Note: We are pleased to serve as agent for a trustee!

Failure to diversify. Laws governing the prudent investment of trust assets vary from state to state. In general, concentration of assets should be avoided. According to many experts, a red flag should go up when any one asset accounts for more than 10% of a trust. Problems with that holding could lead to lawsuits by disgruntled beneficiaries against the trustee. On the other hand, the person who creates a trust may override the diversification requirements. For example, shares in a family business could be exempted from the diversification mandate.

Biased distributions. One of the most important benefits of trust-based wealth management is delivery of financial resources to multiple generations, today and in the future. Trouble is, finding the appropriate balance between current and future interests is not easy. Trustees need to document reasons for allowing or denying invasion of a trust for particular beneficiaries, for example. What's more, the investment strategy chosen for a trust may inadvertently favor some beneficiaries over others. When a family member is a trustee, the issue of bias can become quite emotional.

Expecting a payday. Trustees should be paid, but beneficiaries don't always see it that way. When the trustee is a family member with an interest in the trust, the payment issues can be especially sensitive. Compensation matters should be settled before the trustee assumes the duties of trust management.

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False sense of safety. Some amateur trustees assume that, given their relationships to the family and trust beneficiaries, their work won't be scrutinized closely. Not so. The role of trustee has potentially unlimited liability. Trustees may be called to account for their investment choices, as well as for the quality of their fiduciary judgments about trust distributions.

Consider the professional alternative as your trustee

Given the complexities of modern trust management, one would expect that businesses, such as trust companies and bank trust divisions, would become available to meet the need. One would be absolutely correct! That's us!

Key qualifications that we bring to the table:

- *Integrity.* The single most important qualification for any trustee is … trustworthiness. A trustee must live up to standards higher than those that prevail in everyday business.
- *Investment experience.* A trustee may be called upon to consider the current income needs of a surviving spouse and the capital growth needs of two children who face heavy education expenses in years to come, and then to come up with an investment program that does justice to both requirements.
- *Administrative know-how.* A trustee must make sure that trust assets are properly titled and safeguarded, collect income and distribute or reinvest it as the terms of the trust direct, and perform any number of other chores.
- *Tax and accounting capabilities.* A trustee must be aware of federal and state tax requirements, keep detailed, accurate records and submit timely reports to beneficiaries.
- *People skills.* The ability to serve as a trustworthy financial advisor, both to the individuals who create trusts and the beneficiaries that they name, may not be a formal requirement of trusteeship, but it's important nonetheless.

We offer you our technical skills and our financial and auditing infrastructure for the successful implementation of your trust plan. Most importantly, we offer you our experience as trustee. It's a truism that every wealthy family is different, and so is every trust plan. Yet all trust management is governed by the legal standards of fiduciary duty. We've seen a range of family circumstances, of market environments, of trust purposes and objectives.

Shall we discuss your needs?

We invite you to learn more about our capabilities as trustee for your family. You may designate us to serve as sole trustee, or as cotrustee along with family members. Call on us to discuss the possibilities. ☐

Trustee checkpoints

To make an informed decision about your choice of trustee, think about questions such as these:

- Does the prospective trustee have the time and experience necessary to handle the job?
- Has the organization or individual performed capably in both bull and bear markets?
- Could conflicts of interest arise between your trustee and your family?
- Will each and every beneficiary be treated fairly and impartially?
- What fees will the trustee charge? Do the fees include investment management costs, or will they be an additional expense?
- Will your trustee provide recordkeeping at no additional cost?
- If conflicts develop between the beneficiaries, how will they be resolved? Will all the beneficiaries respect the decisions of the trustee?

Disaster or sound planning?

A celebrity will sparks a debate.

The headline in the New York *Daily News* was a grabber: "James Gandolfini will a tax 'disaster' says top estate lawyer." The conclusion was drawn from a few facts from the will and some major assumptions about the actor's estate.

In the usual case, the primary beneficiaries of a will are a surviving spouse and perhaps children. In that situation, all federal estate taxes may be deferred until the survivor's death. But Gandolfini's was not the usual case. The will provided 30% of the residuary estate to each of two sisters, with another 20% going in trust to Gandolfini's infant daughter. Only 20% of the residuary passed to the surviving spouse, Gandofini's second wife. His home and land in Italy will be held in trust for his children.

That sharply limits the amount of the marital deduction available to shield the estate from inheritance and estate taxes. The *Daily News* estimated Gandolfini's estate at $70 million, and with the marital deduction so severely curtailed, that could mean federal and state death taxes reaching $30 million, according to their consultant.

Few people have that kind of cash available, so the estate would have to sell assets to come up with the tax payments, which are due nine months after death. Such an outcome could prove to be a financial disaster.

Alternative explanations

However, there are clues that there might be more to the story.

Gandolfini's 13-year-old son from his first marriage is mentioned in the will. He receives his father's clothing and jewelry, but no part of the residuary estate because he already has been provided for. An irrevocable life insurance trust was created for the son when his parents divorced, holding a $7 million insurance policy on Gandolfini's life. That trust should not be subject to estate or inheritance taxes, which suggests that the estate plan was constructed with due regard to tax considerations.

The will stated that Gandolfini had made other provisions for his surviving spouse, to explain why she received only 20% of the residuary. The details of those provisions are unknown, but they could include a marital trust or QTIP trust. The inventory of the estate has not been filed as of this writing, and, in particular, the disposition of Gandolfini's royalties from the TV series in which he starred, *The Sopranos*, is not known. Perhaps he already gave those to his wife? Perhaps that was his most valuable asset?

The will was signed on December 19, 2012. That was an intense period for estate planners, because the federal estate tax exemption was scheduled to fall to $1 million at the end of the month. Many wealthy families were taking steps during that month to "lock in" their higher exemption with lifetime transfers. Perhaps Gandolfini did also. It's possible that as a result of such actions, the estate will turn out to be smaller than the early $70 million estimate.

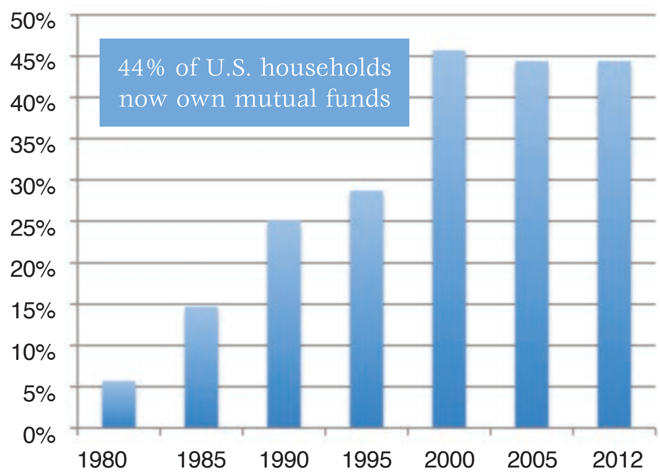
Two mysteries

However, there are two puzzles about Gandolfini's estate plan that are harder to explain. First, the will calls for the payment of all estate and death taxes from the residuary without apportionment. That means the surviving spouse's share effectively helps pay the tax, which further reduces the marital deduction. Very roughly, 20% of a $70 million estate is $14 million, while 20% of an after-tax $40 million estate is just $8 million.

The second puzzle is, why did he not utilize a revocable living trust for implementing his estate plans? All of the dispositive provisions of the will could have been included in a living trust. The living trust has this large advantage over a will: financial privacy. Normally, the trust terms are not made public, but the terms of a will must be. With a living trust, there is a very good chance that the details of a family's financial situation never will appear in the national press—or in financial planning newsletters, such as this one. ☐

Who owns mutual funds?

There are 92.4 million mutual fund investors in the U.S., reports the Investment Company Institute in its *2013 Investment Company Fact Book*. Those investors represent 53.8 million households, or roughly 44.4% of all U.S. households. That level of mutual fund ownership has held steady during this century.



Source: *2013 Investment Company Fact Book*

The explosive growth in mutual fund ownership after 1980 may be attributable to the advent of 401(k) plans. Indeed, for 63% of households their first mutual fund purchase was through an employer-sponsored retirement plan. Some 35% of those who own mutual funds own them only inside such plans. Mutual funds owned in IRAs, which first became widely available in 1981, may also account for this spectacular growth.

As one might expect, as household income rises, the odds of finding mutual fund investors rises also. Some 81% of U.S. households with income over $100,000 are mutual fund owners. Still, mutual funds are certainly not just for the very affluent. Some 22% of mutual fund-owning households reported income of less than $50,000, and the median income of such households was $80,000.

Why invest in mutual funds? According to the survey, which permitted multiple answers to the question, 93% are saving for retirement; 50% hold mutual funds to reduce taxable income; 48% are saving for emergencies; and 27% use mutual funds to save for education. For 68% of these savers, more than half of their financial assets are mutual funds.

U.S. mutual funds grew to $13 trillion in 2012, half of the worldwide total. Domestic and international equity funds composed 45% of the total industry assets, bond funds 26%, money market funds 21% and hybrid funds 8%. ☐