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Trust UPDATE

Stillman BANK

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The CARES Act and your retirement savings

In March Congress responded to the ongoing pandemic with the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). The new law has many facets, but in this article we focus on the effects on your retirement savings.

No required minimum distributions in 2020

When the stock market collapsed during the 2008 great recession, Congress created a one-year suspension of the rule that requires minimum distributions (RMDs) from IRAs and qualified retirement plans. The purpose of the suspension was to avoid forcing withdrawals when values were low, which could dramatically deplete account balances.

Essentially the same rule has been enacted for 2020, for the same reason. Retirees who have already been on a program of required minimum distributions (RMDs) won't have to take one for the 2020 tax year. The same rule applies to beneficiaries of inherited IRAs. Of course, they are allowed to withdraw money if they wish to.

Someone who turned 70½ in 2019 was required to take an RMD for the 2019 tax year but was allowed to defer that distribution until April 1, 2020. If the distribution was taken in 2019 (to avoid having two RMDs in the same tax year) it must be retained. If the distribution was not taken, it is now waived. The IRS provided transitional guidance, under which RMDs taken after February 1, 2020, may be rolled back into an IRA until July 15, 2020. RMDs taken in January 2020 are not eligible, but the stock prices were much higher then anyway. Many people who took withdrawals during that month are happy that they did so, locking in higher values.

These changes apply to all taxpayers, not only those who have been directly affected by the pandemic.

Beginning this year, RMDs are not required until reaching age 72. That change was enacted last year. Additional parts of the legislation address plan loans and COVID-19 distributions. However, these provisions must be adopted by the plan sponsor before they are available to plan participants.

Plan loans

The normal rule for a plan loan from a 401(k) plan or qualified retirement plan is that one may borrow up to 50% of the vested balance, to a maximum of $50,000. These caps are doubled for certain loans made from

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March 27, 2020, to September 23, 2020, to a maximum of $100,000 or 100% of the vested balance. Repayment of the loan may be deferred until January 1, 2021, when a five-year amortization must begin.

The expanded loan rule is available to any taxpayer who tests positive for COVID-19 or whose spouse tests positive. The larger loan may also be permitted for someone who:

- was quarantined, furloughed, laid off, or had reduced hours because of the disease;
- was unable to work because of lack of childcare;
- experienced a closing or reduced hours of a business owned by the taxpayer because of the disease; or
- was affected by other factors that may be identified by the Treasury Department.

Loans are not permitted from IRAs or Roth IRAs.

Coronavirus-Related Distributions

An alternative to the loan is a distribution, which is permitted for the same "qualified individuals" as the expanded loan provision. Up to $100,000 may be distributed. The distribution will be subject to income tax, but there will be no 10% penalty on premature distributions if the account owner is younger than 59½. The income tax may be paid in full for the 2020 tax year (it could be the best choice if the taxpayer has fallen into a low tax bracket). Alternatively the distribution may be treated and taxed as if 1/3 was received in 2020, 1/3 in 2021, and 1/3 in 2022. Deferring the tax bill is tempting, but one may be in a higher tax bracket in two years. Also, the state income tax treatment of the distribution may not match the federal rules.

However, there is an alternative that involves no income taxation at all. The taxpayer may elect to repay the Coronavirus-Related Distribution over three years. Such repayments will be treated as if they were trustee-to-trustee transfers. What's more, the repayments will not affect the taxpayer's right to make future normal retirement plan contributions.

Although these "relief valves" for affected taxpayers are welcome, invading retirement resources should be considered as a last resort, especially when stock prices have fallen substantially. Taking a distribution when values are low may amount to locking in a loss.

We are here to help

If you have questions about the adequacy of your savings or the volatility of your investments, we are available to consult with you. Everyone's goal for retirement is financial independence and security. Financial independence doesn't happen by accident, it takes hard work, discipline, and investment expertise. We would be pleased to share our insights with you. ☐

Who should be your trustee?

Trustee selection is an often overlooked yet critical element of a sound plan for family wealth management.

To paraphrase the words of Jack Webb, of *Dragnet* fame, the story you are about to read is true, taken from a recent court case. The names have not been changed to protect the innocent, they are taken from the legal record.

The will of a bachelor farmer, Jack Fenske, created a trust for the management of his estate. His niece was to receive the trust income for her life, and her daughters, Jennifer and Laura, would inherit that trust income for all of their lives. The trust permitted distributions of principal to pay for the education expenses of the grandnieces, but otherwise did not allow for early invasions. The trust will terminate when both grandnieces die, with trust assets passing to their descendants at that time.

When Jack died in 1998, it happened that his niece had already died as well. Thus, Jennifer and Laura received all the trust income from the moment of its creation. They also received distributions for their education. For example, Laura earned both an MBA and a law degree. Laura married an attorney, David.

In 2017, after some 19 years of continuous support from the trust, David asked the bank trustee to resign. The beneficiaries reportedly were concerned that trust income was too low, and the bank's fees were too high. David was eager to be the trustee. He asserted that as an attorney he was fully qualified for the job, and he promised that he would work for free.

The bank refused to resign the trusteeship because doing so would defeat a material purpose of the trust. The bank stated that a member of the bank's trust committee knew Fenske personally and had some insight into why he set up the trust as he had.

The beneficiaries then took the matter to court. The current income beneficiaries and the future principal beneficiaries all agreed that a new trustee was called for, which in the usual case is enough to cause a change of trustee. Still, the bank resisted.

At the trial, Laura admitted that replacing the trustee was just the first step toward terminating the trust and distributing its assets in a manner not yet determined. The trust at that time contained some $52,000 in a money market fund, a $30,000 note from Jennifer, and farmland valued at about $280,000. The trust had been depleted by $240,000 in principal distributions for education expenses for the two young women. The bank trustee testified that the land was being rented as pasture, and it admitted that the rental income did not reflect the property's development potential. The trustee was open to selling the land to diversify the trust assets, but not to resigning the trusteeship.

What was Mr. Fenske thinking?

The lawyer who drafted Jack's will, Richard Stafford, was also available to testify at the trial. Why did Fenske choose the bank as trustee? For one thing, according to Stafford, Fenske was friends with the bank's President, and it was the only bank in the area that operated a trust department. More importantly, Fenske did not trust his brothers or any other person he knew to not squander his assets. He wanted to keep the estate "together as long as it could possibly be kept together."

The lawyer was asked whether a trustee other than the bank could carry out the purpose of the trust? Was there a reason for limiting the choice of trustee to a bank? The lawyer replied, "No, other than … the one thing I think [Fenske] was really trying to get away from was to have any of his relatives in charge of his assets."

A decision

The court ruled that in cases where the selection of a trustee did not appear to be central to the creation of the trust, the requirements for replacing the trustee are limited. But in a case such as this, given the evidence that Fenske did not want family members to manage his assets, the choice of trustee rises to the level of a "material purpose" of the trust. Even ignoring Laura's admission that she hoped to terminate the trust, the substitution of her husband as trustee would violate the trust terms. Therefore, the request to fire the trustee was denied by the court.

Some might say that after 19 years, heirs ought to be able to receive their inheritance outright. But that judgment is one that is to be made by the trust creator, not by others. Fenske was a careful and prudent man all of his life, and one of the better choices he ever made was the selection of a trustee that would be loyal and fierce in protecting the terms of his trust.

What a trustee does

The management of a trust involves much more than day-to-day investment supervision, important though that is. Trusts typically have several beneficiaries, and these beneficiaries often have interests that are adverse to some extent. They may be of different generations, for example, and their interests in the trust may vest at

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If you've decided against a corporate fiduciary

If you've decided to name an individual as your executor or trustee, reflect upon these questions:

- Will the person also be your beneficiary?
- Do you owe this person money?
- Does this person owe you money?
- Does the person have an unusual need for money?
- Can your beneficiaries trust the person?
- Will the person work well with others?
- Will the person have enough free time to handle the job?

As you can see, there is a potential for conflict of interest and other difficulties when one turns to a friend or family member, even one with excellent credentials.

different times, perhaps years apart. The trustee has fiduciary obligations to each of the beneficiaries, and satisfying these disparate objectives is one of the core responsibilities of trusteeship.

Some trusts permit invasion of principal, either subject to a standard or in the trustee's sole discretion. Some trusts "spray" their income to beneficiaries, in amounts determined appropriate by the trustee. Some trusts include accounting flexibility; that is, items that normally might be credited to principal (such as capital gains) may, should the trustee so decide, be applied instead to income. Decisions such as these are essential to the success of the trust plan.

One might expect the job to be time consuming, and one would be entirely correct. It's understandable that any individual would hesitate to take on the burden of trusteeship when there is an alternative available.

The ability to say no

A trust is, essentially, a long-term wealth management plan created by a trust's grantor. The plan implements the grantor's values and vision. The trustee promises to implement that plan, in a manner consistent with the trust's purposes and instructions?

Does it ever happen that events outstrip the grantor's vision, so that some modifications are needed? Of course. A wide range of developments, from the very good to the very bad, may make the exercise of prudent judgment by the trustee necessary to further the trust's purposes.

Does it ever happen that beneficiaries would like to have the plan modified, because they don't agree fully with the grantor's vision? Yes, that happens as well. It may happen that a beneficiary wants access to trust capital earlier than provided in the trust, or for purposes outside the trust's limits. Very often beneficiaries don't understand fully the benefits of a trust-based wealth management plan. The trust document should address this possibility. Its provisions must be followed to the letter.

What about *your* choice?

Have you nominated a family member to serve as executor of your estate, or as your trustee? Are you confident that they have the ability to handle the job?

We have the skills, the experience and the knowledge to handle properly the job of estate settlement. Trusteeship is our everyday business. We are available and we are impartial. We understand the nature of fiduciary responsibilities, and we know how to discharge them.

And for all this, our fees are generally comparable to what an inexperienced individual would receive. In some cases our experience will help to reduce estate shrinkage, increasing the amount available for beneficiaries.

Would you like to learn more? Please call on us for more details about our estate settlement service. ☐