

Estate Planning

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Trustee Bootcamp: Checklist for the New Trustee

By: Dave Folz, J.D., L.L.L. – Trust Counselor LLC, © February 18, 2021

Following his successful career as a trust officer, Dave Folz founded Trust Counselor LLC, a consultancy advising trustees, especially first-time trustees, on the scope of their duties and responsibilities. When Dave presents these ideas at conferences, he employs a checklist to organize the tasks as well as highlight just how diverse and extensive the duties of trusteeship are. This month's Estate Planning Study is an abridged version of Dave's visual aid for his talks, which is based upon Texas law. For the complete, latest version of the checklist, you may contact Dave at dave@trustcounselorllc.com.

Meeting with the Attorney

- Before meeting with the attorney, read the trust, and all other relevant documents, including removals, appointments, and any releases.
- Ask the attorney about their trust and fiduciary experience. Do they have experience in drafting trusts, modifying trusts, and advising trustees on administrative matters? Ask to be billed monthly. If this is a "special needs trust," be sure they have experience in this area.
- Discuss the purpose(s) of the trust.
- Review the trust terms and their meaning, especially as to who are the beneficiaries, investment powers and restrictions, and distribution standards.
- Verify the beneficiaries (income, remaindermen, a minor, etc.) that may require an accounting.
- Verify other advisors, co-trustees, or trust protectors.
- Ask what a trust accounting is, why it is essential, and how often it must be provided to the beneficiaries?
- What constitutes "material" information that must be provided to the beneficiaries?
- Discuss the differences between principal and income in trust accounting and how that might impact the trust. Note any special treatment for assets such as mineral income, real estate, and hedge funds, etc.
- How long must trust records be maintained? Discuss with the attorney a policy for records retention and destruction.



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- Confirm whether this a generation-skipping trust (multiple generations), whether it is “exempt from generation-skipping taxes” and, if any additional steps, precautions, filings, or taxes are required.
- Ask whether any special tax provisions need attention.
- If any distributions are discretionary, review the process with the attorney.
- Discuss the creation of an investment policy statement. If specialists for investments or other needs are required, determine how they are to be selected and monitored.
- If any of the assets are greater than 5% of the overall assets of the Trust, i.e., single stock holdings, a ranch or family business, ask whether and how to address the issue of diversification?
- Is there real estate held out of state for which an ancillary trustee in that state will be required?
- If the trustee and/or beneficiaries are residents of a state other than Texas, have the attorney or the CPA confirm whether another state will tax the Trust and changes that could avoid that taxation.
- If funding a new trust under a will, ask what date to use for funding valuation purposes—date of death, date of funding, or another date the trust may require. Ask if there will be tax consequences in terms of how the trust is funded.
- Have other conditions changed since the creation of the Trust that may suggest a disclaimer, decanting, modification, merger, termination, or partial distribution?
- Does the trust qualify as a see-through trust or conduit trust for accepting retirement benefits (IRAs, 401(k)s, etc.)? Are there lifetime or testamentary powers of appointment? Are they general or limited; are they specific to assets?
- If the trust “accounting income” is insufficient, can a total return approach be adopted?
- Confirm that trustee’s fees are reasonable and supportable and document.
- Is there a “trust protector?”
- Does the trustee have the right to resign? How does that work? Timing and notice provisions. Who has the power to appoint a new trustee?
- If you are a successor trustee, does the trust require any type of review or not of the prior trustee’s acts? Unless otherwise provided in the trust generally the successor trustee has a responsibility to review on a reasonable basis the acts of the prior trustee.
- If beneficiaries start indicating disappointment, discuss their concerns with the attorney. Do not wait!

Getting Organized: Trust Terms

- Did the grantor convey the purpose of the trust in the trust? Did the grantor provide a letter of wishes or intent? Are the beneficiaries clearly described?
- Is the distribution language for the beneficiaries clear?
- Is there any non-standard investment language?
- Is there retention language for an asset like a ranch or family business?
- For distributions, investments, other trustee decisions, is the direction “may” or “shall”?
- Do other related trusts need to be considered regarding investments or distributions?
- Does the trustee have the right to resign? Before resigning, can the trustee require a release?
- Are there provisions for determining successor trustees if a trustee resigns, dies, becomes incapacitated, or otherwise ceases to serve?
- Confirm with the attorney/CPA whether any special tax provisions need attention.
- Is there a provision for trustee’s fees?
- If there are co-trustees, does the trust indicate which one controls when the trustees disagree? Do decisions have to be unanimous or if there are more than two trustees, does the majority control?
- How long will the trust last, i.e., when does the trust terminate?

Getting Organized: Administrative Steps

- Gather together the original Trust, Amendments, Court Decrees, Family Settlement Agreements, Releases to prior trustees, etc.
- Has the attorney or CPA applied for the Tax Identification Number for the trust?
- Copy of the Federal estate (Form 706) and gift (Form 709) tax returns, if filed?

- Gather together the mailing address, email address, phone number, birthdate, marital and health status of each current and each "vested" beneficiary. Have each beneficiary sign a W-9 confirming their social security number.
- Do any of the beneficiaries have "special needs," supported by Medicaid, or other government programs, etc.?
- Contact information for trust committee members and trust protector (if any).
- Are electronic files backed up appropriately with strong passwords and are the trust records reasonably protected from cyber criminals?
- If this is a pre-existing trust, get the prior years' income tax returns.
- Gather a list of the assets and liabilities with current fair market values.
- If the trust owns real estate, are there verbal or written leases?
- If a trustee must collect personal items at a home or perform an inventory, a witness should accompany the trustee. Check clothing and old books for cash and jewelry. Alternatively, hire a firm that does estate collection/appraisal services professionally.
- Are there any outstanding legal claims by or against the trust (including against the prior trustee)?
- Are all the assets titled in the name of the trust; are there assets remaining to be transferred?
- Do you have the grantor or prior trustee's user names and passwords for an online account?
- Are assets like jewelry, art, high-end cars, protected and insured?
- Are all life, liability, property, and casualty insurance premiums accurately titled, evaluated as to proper coverage, and premiums paid up to date?
- Do all the investments have proper tax cost basis and holding periods identified?
- If assets are coming from the deceased's brokerage account (titled in the name of the executor or a revocable trust), confirm that the brokerage firm has updated the cost basis of the holdings to reflect the date of death values. Often, even if they provided a report, they might not have updated the account itself.
- If non-publicly traded assets like non-traded REITS, hedge funds, private equity funds, etc., are coming from an estate, be sure that your CPA and the fund managers update the date of death cost basis on your respective records.
- Check www.missingmoney.com to be sure there are no "lost" or "escheated" financial assets.
- If the trust has been created as a result of someone's death and the executor has not done so, the grantor's mail should be forwarded to the trustee.
- Review the mail for information for investments that may not be part of a brokerage statement, especially after year-end when 1099s are received.
- If the grantor left firearms as an asset in the trust, the trustee should consult with the attorney as to the many state and federal rules regarding transfer and sale. Criminal penalties may apply if these are not properly handled.
- Open bank and investment accounts in your name as "Trustee for the Trust, Dated....."
- When signing agreements for the trust, always sign as "trustee."
- If you, as trustee, hire vendors and agents to assist you, be sure that they understand the confidential nature of the trust.
- Have ticklers or a calendar been created for critical dates, especially for tax returns, estimated taxes, property, and franchise (if applicable) taxes?
- Do any of the beneficiaries have mental or physical disabilities or substance abuse or other behavioral issues? Does the trust have "special needs" instructions? If so, the rules regarding state aid and assistance are complex. Consult an attorney who specializes in this area.
- Has a meeting with each beneficiary or beneficiaries, collectively, been scheduled.

Meeting with the CPA

- Ask the CPA about their experience with trust accountings and trust tax returns. Do they have experience with 1041s, 709s, 706s, and are they familiar with distributable net income (DNI) and the state's Uniform Income and Principal Act?
- Give the CPA a copy of the trust document and ask the CPA to confirm with the attorney the tax status of the Trust and what future events might change that status.
- Confirm who will request the Taxpayer Identification Number for the Trust from the IRS. Each trust will need a Tax ID Number. You will also need to sign Form 56 identifying yourself as the trustee. If this was a revocable trust and the creator of the trust also has a probate estate, you will probably need to complete a Form 8855 and get a Tax Id for the Estate.

- Establish with the CPA a process for collecting and maintaining accurate records for income, expenses, purchases, sales, and other transactions.
- If the CPA does not already have them, collect the last three years of tax returns, whether for an individual, the estate, or the prior trustee.
- Determine depletion, depreciation, or other reserves for mineral/real estate or other similar assets.
- When and who will communicate the annual accounting to the beneficiaries? Be sure the CPA understands that all current and “vested” beneficiaries will need to receive an annual “trust” accounting.
- If there has been litigation, before any settlement is agreed to, be sure that the attorney and the CPA agree as to any possible tax impact.
- Have an annual tax review with the CPA before the tax year progresses too far. Taxes detract from the net investment return; small efforts here may have a big payoff.
- If the trust has oil, gas, or other mineral interests, be sure the CPA has sufficient experience to deal with these as regards trust accounting and tax matters.

Strategy Questions for Annual Tax Review Meeting with CPAs

- Have any changes in the tax law occurred that will impact the trust this year or next?
- Have there been any substantial changes in the investments of the trust in the current tax year?
- Ask the CPA join in the discussion with the investment advisor?
- Are any significant changes, sales, purchases, cash needs, or distributions, anticipated this year or next?
- Have any beneficiaries died or are in poor health?
- If income is insufficient due to the investments and the trustee is not a beneficiary, can principal/capital gains also be paid out from the Trust using the adjustment power?
- Have the tax brackets or the state of residency of the beneficiaries, the trustee, or the state of administration changed since the previous year and is that relevant to the Trust?
- If the Trust has an interest in a Partnership or LLC treated as a partnership, are gains, losses, or income anticipated? Will there be enough cash to cover? Who controls distributions from these entities?
- If the trust is an irrevocable grantor trust, can assets with a low/high basis be swapped with the Trust?

The Trust Investment Process and Strategy

- What are the goals of the trust?
- Does the trust have any specific investment guidelines? Does the state’s trust code have specific investment guidelines for the trust?
- Does the trust require or suggest the retention of certain assets? Is the retention clause specific, meaningful, and unambiguous?
- Is there a significant concentration in any asset or type of asset? Does the trust permit it?
- Are there plans for diversification?
- Are there assets or liabilities that need attention—real estate, mineral properties, drawdowns from retirement accounts, privately held businesses, or private equity funds requiring future capital commitments?
- Are there “hedge funds” that are locked up for extended periods?
- Are the investment interests of the current beneficiaries to be favored over the remaindermen?
- Is there a need for cash near term or in the future?
- Are the liquid funds invested?
- If the trust has substantial unrealized capital gains, is there a strategy to manage these?
- Are there unusual risks to any assets? Have steps been taken to mitigate?
- Are there assets with an expiration date such as copyrights, licenses, or commercial leases?
- In setting the investment goals, have general economic conditions, the possible effect of inflation or deflation, the role that each investment or course of action plays in the overall portfolio, the expected total return from income and appreciation, the other resources of the beneficiary, the need for liquidity, the regularity of income and preservation or appreciation of capital, and an asset’s special relationship or value to the trust or beneficiary been considered?
- As the trustee, do you have sufficient experience to manage the trust assets or do you need to hire advisors?

- Have you researched the advisor's expertise and is their fee reasonable?
- Will the advisor manage under a "suitability" (traditional stockbroker) or a "best interest" (registered investment advisor) standard?
- Is a tickler in place to insure consistent periodic reviews? Banks and regulated trust companies are required to review the investments at least once a year.
- For security trades, i.e., stocks and bonds, for tax purposes most brokerage firms will treat on a First In/First Out basis. To better manage capital gains, it will generally be preferable to use the "specific identification method," the highest in/first out (HIFO), or other brokerage firm elections that may be available. Confirm with the CPA and the financial advisor the best approach to manage capital gains.
- Have the goals of the trust, the time horizon, the risk tolerance, the investment objective, the asset allocation, retention of special assets, distribution and liquidity needs, tax considerations, any unique circumstances, and how performance is evaluated been documented in an Investment Policy Statement?

Reviewing a Trust Securities Portfolio

- Is the asset allocation appropriate?
- Are the assets diversified?
- Has the trust been actively managed?
- Has investment performance been properly calculated?
- Has a relevant, standard benchmark(s) been determined for performance comparisons based on quarter and year-end numbers?
- Has the trust been managed in a tax-aware manner?
- Are the fees reasonable?
- Other than bonds in a designated "high yield" mutual fund, are all bonds investment grade?
- If mutual funds are used, is the share class ("a," "b," "i," etc.) appropriate?
- What are the professional designations and the experience of the investment manager or financial advisor? Check the history of a stockbroker at <https://brokercheck.finra.org/>.
- Check the history of a registered investment advisor at <https://adviserinfo.sec.gov/>.
- Ask the advisor if any arbitrated claims were removed from their FINRA/SEC/State report.

Discretionary Distributions

STEP ONE

- Is this distribution in line with the goals of the trust? Have the distribution standards and purposes of the trust been discussed with the beneficiary?

STEP TWO

- The trust agreement controls discretionary distributions. Discretionary distribution language in early sections of the trust may be modified by definitions in later sections of the trust agreement. Do not hesitate to ask the attorney for help.

STEP THREE

- If the beneficiary requests a distribution, best practices suggest that, it should be in writing, stating the purpose, the amount, the date(s) needed, whether this is one or a series of needs, providing receipts, bills or estimates, and other supporting documents that you or the trust may require (budget, balance sheet, tax return, or statement of other resources or income).

STEP FOUR

- Is there a co-trustee who must concur?

STEP FIVE

- Document, respond, and communicate without unnecessary delay.

Other Considerations

- Is the beneficiary aware of the income tax implications of a distribution of trust income?
- Will the distribution be setting a standard for years to come? For several generations?
- Will the distribution require the beneficiary to show personal responsibility or financial ability to manage the funds after they are distributed?
- Will this distribution be to the beneficiary or paid to someone for his/her benefit?
- Is the distribution from income or principal?
- What is the size of the distribution relative to past requests and the overall size of the trust?
- Is this a fair distribution relative to other beneficiaries or will it unduly favor this beneficiary?
- Instead of a distribution, would it be better to loan funds to the beneficiary or to guarantee a loan/mortgage to the beneficiary?
- If you need financial information from the beneficiary and they fail to provide it to you, document your attempts to do so.
- For beneficiaries with spending challenges, consider hiring a Financial Therapist licensed by the Financial Therapy Association (FTA). While not specifically a trustee responsibility, for elderly beneficiaries, a trustee might look into eldercare, home health care, or geriatric care managers.
- Standards such as “comfort,” “happiness,” “liberally interpreted,” or “best interests” can be broadly interpreted. Consult with the attorney in understanding these and any other unusual standards.
- If the trust is a “special needs trust,” the beneficiary may be entitled to multiple forms of state aid and it will be important to retain an attorney who specializes in this area to assist with a dizzying array of programs and requirements.

Meeting the Beneficiaries, Managing Expectations, Keeping them Informed

- Tensions often exist between trustees and beneficiaries. Meetings are an excellent way to meet, ask questions, and explain the purpose and the benefits of the trust and to build trust.
- If possible, have a face-to-face meeting. With multiple, geographically dispersed beneficiaries, consider using WebEx, Zoom, Skype, or other technology.
- Before the meeting, provide the beneficiaries with an agenda so that they know what items will be discussed and what your goals are for the meeting. Consider working with the beneficiaries on a “mission statement” for the trust.
- Be sure the beneficiaries have a copy of the trust.
- At the meeting, review the trust, the purpose and the goals of the trust, explaining the benefits of the trust, the distribution standards, the levels of beneficiaries, the potential length of time for the trust (their lives, 100 + years, etc.).
- Be sure that each beneficiary has a chance to ask questions.
- Review the investment policy statement for the trust.
- Review the trust investments, their performance, and the trust financial statements for the year.
- Review any significant risks, issues, or plans that the trust might have.
- Confirm how they are to contact you, weekdays, turnaround times, and give them notice when you are on vacation.
- Remind them that if their circumstances change, financial or otherwise, they must notify you.
- Document the meeting (“minutes”) and ask the beneficiaries to confirm.
- Privacy issues are important. Obtain written consent to talk with beneficiaries’ lawyers, accountants, and other professional advisors and obtain permission to communicate with beneficiaries and their advisors via email. Should any of their advisors receive quarterly or annual reports?
- While trust codes generally do not require annual meetings, they build goodwill and trust and help to ensure that “material” matters to the trust are covered (like an annual physical).

Communicating with the Beneficiaries about Family Values

- Transferring family values is extremely hard (James Hughes, Family Wealth, 2004).
- Properly understood, a trust can be a launch pad for a beneficiary to have a more fulfilling life.
- Start early—periodic allowances might be equally saved, shared with charity, and spent.
- For younger or financially unaware beneficiaries, provide periodic financial education.
- Encourage the beneficiaries to work on their estate plans and philanthropy.
- Family meetings and a shared charitable purpose through a family foundation or donor-advised fund can help in this process.

Trust Account Requirements

- A trustee is under a continuing duty to share with a beneficiary all material matters of the administration of the trust, known by the trustee, that might affect the beneficiary's rights. The trustee should not wait to disclose these until the beneficiary asks for an accounting. Review the trust agreement and your state's trust code for specific accounting requirements.
- Material matters to be disclosed may include hiring/firing agents with an important responsibility, significant changes in investment strategy and litigation updates.
- Part of the broad duty of disclosure is to maintain records and to permit reasonable inspection.
- Classes of beneficiaries who are vested and entitled to accountings will depend on the trust agreement.
- Review this with the attorney.
- Alternative investments—distinguish between income and principal, if necessary.
- Accountings for minors should be sent to their parent(s) or guardian.
- CPAs often provide a "compilation" which is somewhat like an accounting. Be sure fair market values are used for the assets in an addendum to the report.
- The accounting should show the ending balance of the prior accounting, which should match the beginning balance on the next accounting.
- Try to avoid using manual systems; human errors can easily pop up!
- Real estate and partnerships should be described by investment type (and location for real estate).
- Personal property (art, jewelry, cars, and other collections) should be described and how they are held for safekeeping.
- Confirm that taxes have been paid.

Trustee Risk Management

- Risks, known and unknown, always exist. New trustees generally do not appreciate their potential liability. Litigation is expensive and judges and juries do not always understand complex trust issues. Generally, unless the trust agreement provides otherwise, trustees can be held personally liable.
- Document, document, document.
- Anticipate and mitigate known future risks.
- Advise beneficiaries of upcoming material changes in the investments, the sale of real estate or a business, or in the administration of the trust.
- When you communicate by voice, letter, or email, assume that someday these may be replayed to a jury.
- Before accepting the appointment as trustee, review with the attorney any exculpation clauses in the trust and their potential effectiveness.
- Purchase trustee errors and omissions insurance, including cyber liability insurance, if reasonably available. Carefully review exclusions.
- When in doubt about a course of action, depending on the circumstances, seek legal advice, the advice of the proper court, or approval of the vested beneficiaries.
- Beneficiary consents, waivers, and releases need to be all-inclusive as to all possible issues and done with full information on the part of the beneficiary. The beneficiary should be represented by their legal counsel.
- Join an association that provides ongoing trust education such as the Independent Trustee Alliance, <https://www.trusteealliance.com/>
- Indemnities from beneficiaries are only as good as their financial condition.

NEVER

- Comingle trust assets with your assets.
- Use trust assets for yourself or your family.
- Hire relatives or other affiliated parties to perform trust services for the trust.
- Invest trust assets in your business or in deals that benefit you.
- Take advantage of an investment opportunity that was made available to the trust.
- Borrow from the trust unless the trust allows and then follow your trust code rules!
- Buy, sell, or lease assets to/from the trust.

- Engage in a competing business.
- Sell a service to the trust.
- Fail to obtain appropriate casualty and liability insurance for trust assets.
- Make an unexplained distribution.
- Fail to file a tax return, pay taxes or miss a reporting deadline.
- Make improper investments.
- Accept anything more than a nominal gift from those doing business with the trust or from a beneficiary.