RALPH MINTO, JR. & ASSOCIATES & WEALTH MANAGEMENT ROUNDTABLE PRESENT

So Your Client Has Been Named As An Executor or Trustee, or, Why No Good Deed Goes Unpunished!

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Executors' and Trustees' Duties

The duties of a trustee and an executor are similar in many ways.

1. Both are governed by statutes.
2. Both impose civil liability upon the fiduciary for the failure to properly carry out the position.
3. The duties of both are almost entirely misunderstood by the public.

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Trustees and Executors
The Untold Stories

Most of you either have, or will have, clients that, because of their standing in the family, have been named as either the executor or the trustee of a relative's or friend's will or trust. Most certainly they will have been named executor of their spouse's estate. They have said yes to these positions because they feel they owe it to these people for one good reason or another.

As their financial advisor, this may be a benefit to you because this will increase your assets under management. The decision to use you seems simple enough, you helped them get where they are today so why not use you for this job. However, you must approach this new responsibility with your client with significantly more caution than might otherwise seem appropriate at first glance.

The pages that follow outline some of the most common problems associated with trust and estate investment and the problems inherent in being a fiduciary.

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Problem Number 1
How much should your client charge for his/her services as fiduciary?

Your client should discuss this up front with the friend or relative who is naming him as trustee or executor. It is my recommendation that your client charge a full and fair price for this work and not, under any circumstances, do the work at a reduced rate or for free. The reason for this will become obvious as we go through these slides.

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Problem Number 2
Has your client, the fiduciary, reviewed the trust document for guidelines on distributions?

Most individuals take on the responsibility of being trustee without ever having even reviewed the document. They don't even have a clue of the circumstances into which they are walking.

1. Does the trust allow for discretionary distribution of either income or principal?
2. If it does, are those guidelines clear and easy to follow or cryptic and difficult?
3. How long is the corpus held in trust?
4. Does your client have counsel to assist him with the administration of the trust?
5. Have investment guidelines been provided for the fiduciary?
6. What are the provisions for the replacement of the fiduciary?
7. What are the current relationships, if any, between your client and the beneficiaries of the estate or trust?

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Problem Number 2, continued.

- What your client probably does not realize is that he, more likely than not, is going to become the focal point of the beneficiaries' financial lives.
- Moreover, whether he likes it or not, will have to make decisions regarding distributions from the trust that are going to make him quite unpopular with the beneficiaries.
- Even further, these decisions could end up with your client being the subject of a lawsuit attempting to compel the distribution of assets from the trust.
- This position will become even more untenable when the beneficiaries come to realize that your client's "huge attorney's fees" are being paid by the trust while their attorney fees, even if they are successful, are not.
- Arguments between fiduciaries and beneficiaries regarding distributions from trusts and estates can become quite expensive and contentious.
- More likely than not, your client, if he had in the past, will not continue to be invited to family birthday and Christmas events. He will, however, most likely be the subject of considerable conversation at such events.
- Consequently, your client should insist on reading the trust document, understand what is being asked of him regarding trust distribution, and if necessary, demand corrective measures be implemented in the trust language if necessary to add needed clarification of murky points. Even this, however, may not correct all problems.

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Problem Number 3
What are the correct types of investments?

The fiduciary must always remember one thing: There will always, I repeat always, be a conflict between the current income beneficiaries and the remainder beneficiaries of a trust regarding how the trust assets should be invested and the trustee who is not aware of this conflict or who chooses to ignore it, does so at his own financial peril.

WHY?

Income distributions are made to the current income beneficiaries while increases in the value of the capital inure to the benefit of the remainder beneficiaries. Remainder beneficiaries generally are those who take after the death of the current income beneficiaries. Thus remainder beneficiaries would rather have the fiduciary invest in items that provide for long term growth (i.e., produce non-distributable long term capital gains) while income beneficiaries would rather have the fiduciary invest in items that produce significant current income (i.e., items that generate interest, dividend income or rents).

Generally the fiduciary must find some common ground between the two. However, finding this common ground is no easy task and complicates investment alternatives immensely. Moreover the penalty for misjudging this investment risk can be personal liability for the trustee. Such liability will come in the form of a lawsuit initiated by a beneficiary (at perhaps some distant time in the future) who, with benefit of hindsight, believes the fiduciary made bad investment decisions.

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Problem Number 3, continued.

The problem of the correct type of investments is further compounded by the recent decisions of the Commonwealth of Pennsylvania courts.

As an example, let's examine a recent case:

In re Schiedmantel, Appeal of Trustee Sky Trust, N.A., This is a decision handed down on January 5, 2005.

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Problem Number 3, continued.

The facts are as follows: The trustee, after acquiring the assets from the estate, decided to diversify the trust holdings from a very large position of the stock of Sky Trust. It viewed the holding both as a conflict (holding a large position in stock of its parent company) and as a non-diversification problem (holding a large portion of the trust in only one stock).

The trustee, therefore, sold off the concentrated stock position, and, with the proceeds, acquired its proprietary mutual funds that had appreciated from the date of acquisition to the date of the lawsuit.

The trust explicitly granted the trustee absolute discretion over investment decisions and exculpated the trustee from liability except in the case of “gross negligence”.

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Problem Number 3, continued.

Notwithstanding these issues, the court found that Sky Bank had violated its fiduciary duties to the beneficiaries and surcharged the bank for losses that had occurred as a consequence of the sale and reinvestment. The court looked at many factors in rendering its decision. These are beyond the scope of this discussion. This case is raised simply to present the point that what seems to be correct at the time may turn out to not be the case in the future and a trustee, who decides to invest funds on behalf of the trust, **must** understand the legal ramifications of these actions. Failure to understand these ramifications can easily result in personal liability.

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Problem Number 4 The trustee can not delegate his personal responsibility!

One of the most common problems encountered with individual trustees is their belief that they can avoid personal liability by obtaining professional investment advice in making fiduciary investment and other legal and financial decisions. This simply is not true. While this argument may go a long way in attempting to prove that the fiduciary acted prudently in obtaining competent financial, accounting, tax and investment advice, a failure by one or more these professionals will ultimately be borne by the fiduciary. The fiduciary's only recourse then is to sue the professional for malpractice, etc.

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Problem Number 5 Confidentiality versus the public accounting.

Under the laws of the Commonwealth of Pennsylvania, fiduciaries remain personally liable for their actions as fiduciaries until they file a formal accounting with the probate court. Such formal accountings may be filed at any interval chosen by the fiduciary. Informal accountings to the beneficiaries will not toll the statute of limitations on actions against the fiduciary.

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Problem Number 5, continued.

Most fiduciaries are not aware of this provision. Those that are do not comprehend its effect on their work. Most don't believe the trust should incur the cost associated with formal accountings. These accountings can be costly. **Your clients should always file annual fiduciary accountings. It's a good habit and it's the right thing to do.**

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What then, is your recommendation?

1. Clients should carefully consider the role of fiduciary.
2. If they decide to take the role, they should insist on proper compensation.
3. They must have experienced and competent legal, accounting and investment professionals who understand the roles played by fiduciaries.
4. You should interview professional fiduciaries and review their charges and the benefits they provide before looking to a friend or relative to serve as a fiduciary.

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Thanks for Attending!

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