

Family trusts branch out Multiple advisers divvy up trust duties

By [Nora Lockwood Toohar](#) Staff writer

Centuries ago, the nation's wealthiest families left their heirs empires of oil, railroads and steel.

But today, many family trusts are invested in stocks, hedge funds and real estate developments. And they're no longer relying solely on the staid neighborhood bank to manage their wealth.

Instead, many are hiring investment managers to aggressively build their trust portfolios, while naming others to take care of the paperwork and distribute money to family members.

Spurred by changes in state laws that authorize the use of multiple advisers to manage trust portfolios, the stodgy family trust is modernizing. Many states have passed statutes which allow trusts to divide duties between co-trustees and advisers. Some states also allow trusts to designate a "trust protector," with the power to replace trustees.

"In the days of yore, a trust was used to hold the family land. Today, the trust is used to hold a portfolio of liquid financial assets, which requires more active day to day management," said Robert Sitkoff, a trusts and estates professor at Harvard Law School.

"There's little reason to assume that one person or one organization is going to excel at all aspects of trusteeship," he said. "You might use a bank or other institutional trust company because of its experience in portfolio management or administration, but you might name a trust protector who can override the trustee on issues of distribution.

"We're seeing the use of multiple people or entities in the trustee box because the trustee box is being asked to do more and more," he said.

Joan Crain, senior director of wealth management strategies at BNY Mellon Wealth Management in Fort Lauderdale, agreed: "Today there's a greater diversity in the types of assets that you get through trusts - family businesses, a lot of real estate. ... There's also concentrated stock from family businesses that went public, so maybe 75 percent of the stock will be in that company, and the trustee isn't comfortable holding it."

There's another possibility, she said: boutique investments.

"The wealthy are likely to have some of their assets managed by commodities managers or hedge funds, and that makes corporate trustees uncomfortable. Any trustee who doesn't specialize in that area would find it difficult to properly manage them," Crane noted.

Directed trusts

Experts estimate that by the middle of this century, the largest intergenerational wealth transfer in the United States - more than \$41 trillion - will have taken place.

Competing to capture the lucrative family trust business, states are revamping their trust statutes to offer tax breaks and encourage the use of multiple trust advisers. So far, 20 states have adopted the Uniform Trust Code, which allows trustees to delegate duties to co-trustees and agents, and generally provides that trustees are exempt from liability for others' actions, except in cases of a "serious breach of trust."

About 10 states have adopted "directed trusts" statutes that specifically authorize the appointment of co-trustees and advisers for investment, management and distribution duties.

South Dakota and Delaware, which are considered to have the strongest directed trust statutes, eliminate liability for a trustee who follows instructions from an adviser appointed in the trust agreement to make investment or distribution decisions.

Peter S. Gordon, a trusts and estates lawyer and principal at Gordon, Fournaris & Mammarella in Wilmington, Del., said directed trusts are ideal for family trusts heavily invested in the stock of a family company that long ago went public.

"You've got a lot of trusts that are over-concentrated, with 90 percent of their value, for example, in stock that is now publicly traded. Often, fiduciaries don't want to administer that because they're worried the stock price will plunge and the family will sue," he explained.

"You could move that trust to Delaware, appoint a Delaware corporate trustee and reform the trust as part of the move so that the trustee will only sell the stock upon the written direction of the investment direction adviser, who is usually a member of the family, often the patriarch or matriarch," he said.

"The corporate fiduciary knows they can administer the other 10 or 15 percent of publicly traded securities, but ... they don't have to worry about being sued for not diversifying," Gordon said.

Most of the directed trusts moving to Delaware are family trusts with more than \$10 million in assets. One advantage to clients is that appointing a bank or other institution solely as an administrative trustee reduces corporate trustee fees.

According to Gordon, administrative trustees generally receive annual fees of \$3,500 to \$10,000 per trust, rather than fees based on the value of the trust. On the other hand, a complex family trust that uses multiple advisers may actually end up paying higher fees.

In addition to an investment adviser, a trust may appoint a distribution adviser, such as a family member who ensures that funds are not distributed to any family member who, because of drug or alcohol addiction, for example, is unable to handle the money.

Bruce Stone, a trusts and estates lawyer and shareholder at Goldman, Felcoski & Stone in Coral Gables, Fla., said directed trusts can also be used for running closely held family businesses.

"A corporate trustee doesn't want to get involved in running a closely held business, and families don't want corporate trustees interfering in a lot of their decisions," he commented. "The solution is that with a directed trust, the corporate trustee only has to do certain things."

Crain, of BNY Mellon Wealth Management, agreed: "The family wants a corporate trustee to do all the important things - like tax returns, compliance - so the directed trust is the answer, because by statute, you can relieve the trustee of liability and responsibility for holding those assets."

Crain is the chair of a Florida Bankers' Association Trust legislative committee, which expects to introduce a bill next year proposing a directed trustee statute in Florida.

"It's a competitive issue," she said. "I personally have lost trust business because Florida doesn't have a directed trustee statute."

Florida's existing trust laws "don't go far enough in insulating a trustee," Crain said.

"You still have the duty to oversee, to monitor, to intervene," she noted. "The directed trustee statutes in the few states that have strong ones are explicit as to the lack of responsibility on the part of the trustee for reviewing the actions of the investment manager."

Ethics debated

But Stone, who is a member of Crain's committee, said he is concerned about statutes such as Delaware's that exempt trustees from all liability for co-trustees' and agents' actions.

"If I'm the directed trustee of a marital deduction trust in which the spouse is the exclusive beneficiary, and I get a direction from an individual distribution trustee to pay money out of that trust to an adult child, I know that's a violation of the trust. Should I be exempt from liability?" he asked.

John P.C. Duncan, the principal of a trusts and estates law firm in Chicago who helped draft recent legislation modernizing New Hampshire's trust laws, said in researching trusts with multiple agents he identified several problems, "not the least of which is that these people didn't seem to have any duty to each other.

"They didn't have a responsibility to even communicate to each other what they were doing," he remarked.

New Hampshire's trust statute requires each mini-fiduciary - anyone who holds power over trust actions - to communicate important actions that affect other trustees

and agents.

"If I am the trust adviser and I want to lock up a big chunk of the assets in some hedge fund where I can't get them out for a couple of years, I better let the trustee who makes the distributions know," Duncan explained.

On the other hand, New Hampshire's statute makes it clear that if a trust agreement gives a specific duty to a trust protector or adviser, the corporate trustee no longer has that responsibility.

"The trustee is exempt from liability for actions or omissions of a trust adviser, but that duty to communicate is still there," he said.

Family trusts leave home

According to Sitkoff, two other statutory changes are transforming family trusts:

** Total return investment approach.*

All 50 states have adopted modernized trust investment laws, which recognize that since the early 1990s trusts have become more heavily invested in stocks and corporate securities.

** Abolition of the rule against perpetuities.*

Twenty two states have abolished the rule as applied to interests in trusts, which minimizes the tax consequences as trusts are transferred from generation to generation.

Over the past 20 years, about \$100 billion in trust assets have poured into the states that have abolished the rule.

"It's an example of the competition between the states to attract trust business," Sitkoff said.

The changing landscape of state trust laws has created quandaries for trusts and estates lawyers who traditionally help clients set up trusts in their home states. Should an attorney based in Illinois, for example, advise a client to consider a directed trust in Delaware?

"This is not an easy issue to deal with," Duncan said, "but trusts and estates lawyers around the country are increasingly aware of the best laws and jurisdictions in other states, and are finding the right way to help their clients with the opportunities those laws create."

Questions or comments can be directed to the writer at:
nora.tooher@lawyersusaonline.com