Trustee Bootcamp

Checklists for the New Trustee!

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1.

WHAT DOES IT MEAN TO BE A TRUSTEE?

TRUSTEE = FIDUCIARY BLACK'S LAW DICTIONARY

One who owes to another the duties of good faith, loyalty, due care, and disclosure;

Someone who must exercise a high standard of care in managing another's money or property.

US SUPREME COURT

Justice Cardoza (*Meinhard v. Salmon*, 1928), Standard for a Fiduciary

Something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior.

TRUSTEE DUTIES

DUTY to collect, preserve, and maintain trust property

DUTY to administer the trust according to its terms

DUTY to make trust assets productive

DUTY to invest prudently

DUTY to provide an accounting

DUTY to disclose material facts

DUTY of skill and care

DUTY to keep trust assets separate

DUTY to avoid self-dealing – loans, purchases/sales from and to the trust or using trust property

DUTY to avoid conflicts of interests

DUTY to enforce and defend claims

DUTY to give notice

DUTY of impartiality

DUTY of loyalty

DUTY of confidentiality concerning the trust and the beneficiaries

2. DOCUMENT DOCUMENT DOCUMENT

3.

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? Board Certification in Estate Planning and Probate by the State Bar is a plus. Ask to be billed monthly.
- ☐ 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. Income is generally interest, dividends, rent, and royalties. Principal is described as the assets of the trust and their capital gains and losses. 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.
- ☐ 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. Is there a designated tax advisor or tax trustee?

MEETING WITH THE ATTORNEY (continued)

- ☐ 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 10% 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? Who will manage the property?
- ☐ If the trustee and/or beneficiaries are residents of a state of other than Texas, have the attorney or the CPA confirm whether another state will tax the Trust and changes that could avoid that taxation (the US Supreme Court heard this issue recently, North Carolina Dept. of Revenue v. Kaestner, and on the particular facts decided in favor of the Trust, June 21, 2019). State income taxes on trusts vary widely depending on where the trustee lives, where the beneficiaries live, and where the trust is managed. Consider whether the trust situs or the trustee needs to be changed.
- ☐ If funding a new trust, which is not the residuary of the estate, 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.
- ☐ If any of the assets have a very low tax basis, how is that to be managed?
- ☐ Does the trust need to be modified in any way to accommodate the tax situation of the beneficiaries?
- ☐ 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.)?
- ☐ If the Trust owns Sub S stock, does it have QSST or ESBT language to accommodate those holdings?
- ☐ If this is a Grantor Retained Annuity Trust (GRAT), which owns public stock, be sure that all securities filings and rules are followed. You may need to retain special legal counsel for this.

MEETING WITH THE ATTORNEY (continued)

- ☐ Are there a lifetime or testamentary powers of appointment? Are they general or limited; can they be specific to assets?
- ☐ Does the trustee need to disclaim any assets?
- ☐ If the trust "accounting income" is too low, can a total return approach be adopted under Texas Trust Code/IRS regulations?
- ☐ Confirm that trustee's fees are reasonable and supportable and document.
- ☐ Review the following checklist on trust terms with the attorney.
- ☐ If you are a co-trustee or a "directed trustee" (per the Texas Trust Code Section 114.0031), what are your responsibilities as concerns the actions of the other trustee(s) or others with the power of direction?
- ☐ 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 beneficiaries start indicating disappointment, discuss their concerns with the attorney. Do not wait!
- ☐ Are there any other questions?

4.

GETTING ORGANIZED: TRUST TERMS

- [ ] Read the trust carefully, ask questions!
- [ ] Hi-light unusual language for future reference.
- [ ] Is the Trust's "domicile" in Texas? Does the Texas Trust Code apply?
- [ ] Did the grantor convey the purpose of the trust in the trust? Did the grantor provide a letter of wishes or intent?
- [ ] Do you understand the difference between "principal" and "income" in trust accounting and its importance in this trust?
- [ ] Are the beneficiaries clearly described?
- [ ] Is there an adopted child or child born out of wedlock and do they qualify as beneficiaries?
- [ ] 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?
- [ ] Does the Texas Uniform Prudent Investor Act apply or is it waived?
- [ ] 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.
- [ ] Can the trust lend to the trustee, the beneficiaries or related entities, estates, or trusts? If to the trustee, does the loan meet the criteria of Texas Trust Code Section 113.052? Is the loan properly documented?

GETTING ORGANIZED: TRUST TERMS (continued)

- [ ] Can the trust be a guarantor of third-party loans to beneficiaries or related entities, estates, or trusts?
- [ ] Can trust buy or sell to the grantor's estate, other related trusts, or beneficiaries?
- [ ] 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? What is the Rule Against Perpetuities? Who are the measuring lives?
- [ ] Does the trust have “spendthrift language" that protects the trust against creditors of the beneficiary?
- [ ] Does the trust reference the separate property of the beneficiaries?

5.

GETTING ORGANIZED: ADMINISTRATIVE STEPS

- [ ] Gather together the original Trust, Amendments, Court Decrees, Family Settlement Agreements, Releases to prior trustees, etc.
- [ ] Are there prior trustee resignations and successor appointments? Do you have the documentation?
- [ ] Has the attorney or CPA applied for the Tax Identification Number for the trust?
- [ ] Copy of the Federal estate (Form 709) and gift (Form 706) 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" (a legal term), supported by Medicaid, etc.?
- [ ] Contact information for trust committee members and trust protector (if any).
- [ ] Are electronic files backed up appropriately with strong passwords? Does the successor trustee or the attorney/CPA have the name and password in case of disability or death of the trustee?
- [ ] 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 the trust owns producing mineral properties, locate the division orders, be sure that the trust is being properly paid, and the producer has the proper paperwork to insure continued payment to the trust.
- [ ] If the trust owns partnership interests, is there a written agreement?
- [ ] With any real estate, are there any known environmental issues and have you inspected the property?

GETTING ORGANIZED: ADMINISTRATIVE STEPS (continued)

- [ ] If a trustee must collect personal items at a home or perform an inventory, another person to witness the process should accompany the trustee. Be sure to check clothing and old books for loose cash. 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), confirm that the brokerage firm has updated the cost basis of the holdings to reflect the date of death values. Even if they provided a report, they might not have updated the account itself.
- [ ] If the brokerage account is used for distribution purposes, be sure that the purpose and name on the check are on the distribution/withdrawal line in the brokerage statement.
- [ ] Have non-liquid investments, such as real estate and business interests, been independently valued as to fair market value?
- [ ] If the trust owns life insurance policies, have these been appraised and reviewed. Should they be retained or sold?
- [ ] For missing life insurance policies, for a national search, go to https://www.naic.org/documents/consumer_alert_locate_lost_life_insurance_benefit.htm
- [ ] Do a check at www.missingmoney.com to be sure there are no “lost" 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.

GETTING ORGANIZED: ADMINISTRATIVE STEPS (continued)

- ☐ 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. Depending on the trust, you may want to ask any trust employees, vendors, and agents to sign a non-disclosure agreement (NDA).
- ☐ Have ticklers or a calendar been created for critical dates, especially for tax returns, estimated taxes, and property taxes?
- ☐ Do any of the beneficiaries have mental or physical disabilities or substance abuse or other behavioral issues?
- ☐ Has a meeting with each beneficiary or beneficiaries, collectively, been scheduled?
- ☐ Has a successor trustee been appointed in the event of disability or death of the first trustee?
- ☐ Does the successor trustee have user names and passwords for electronic files?
- ☐ In Texas, a trustee must perform its trust duties as an individual, not through an LLC or other corporate entity (unless that entity is approved through the Texas Banking Commissioner).

6.
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 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.
- ☐ Confirm with the CPA the different tax deadlines for trusts and whether quarterly estimated taxes will be due.
- ☐ Determine depletion, depreciation, or other reserves for mineral/real estate or other similar assets.
- ☐ Does the accountant's tax software have defaults that are inconsistent with the state's trust code or the trust agreement, i.e., it defaults short term capital gains to income?
- ☐ If the trustee is a resident of a state of other than Texas, have the attorney or the CPA confirm whether another state will tax the trust and changes that could be considered.
- ☐ As to trust-owned real estate, is there an agent in place to protest property values as to property taxes? If not, does the CPA have recommendations?
- ☐ If the trust owns a privately held business, is it a Sub-S and is the trust an electing small business trust "ESB"), a qualified Sub-S trust "QSST"), a grantor trust, or another type of trust allowed to own Sub-S stock?

MEETING WITH THE CPA (continued)

- ☐ Annually, discuss paying the annual net income from the prior year within 65 days of the end of the tax year of the trust to the beneficiaries (Sec. 663 (b) election, page 2 of Form 1041).
- ☐ Often it seems, the initial 1099s from brokerage firms and mutual funds for the previous tax year are amended and new ones sent out. Ask the CPA what the best time is to start forwarding 1099 info for tax return preparation.
- ☐ If it is necessary to separate income and principal (Texas Uniform Principal and Income Act, Chapter 116 of the Texas Property Code), confirm that the CPA will do.
- ☐ If the CPA is preparing an accounting or an annual financial statement, confirm the timing.
- ☐ 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.
- ☐ Before the termination of the trust and distribution of the trust assets, have the CPA review the last three years of tax returns.
- ☐ 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.
- ☐ Does the CPA, lawyer, or financial advisor have a “shared portal" for crucial documents?
- ☐ Have an annual tax review with the CPA before the tax year progresses too far. Taxes detract from the <u>net investment return</u>; small efforts here may have a big payoff.
- ☐ Discuss with the CPA “Direct Pay" options for taxes with the IRS (and states, as necessary).
- ☐ If the trust is receiving assets from an estate in its final tax year, confirm that the CPA is current on the deductibility of those expenses by the trust (Proposed Regs, IR-2020-90, May 7, 2020).
- ☐ If the trust has or intends to purchase Master Limited Partnerships (MLPs), ask what the additional charge will be for preparing the trust tax return.
- ☐ 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.

MEETING WITH THE CPA (continued)

Strategy questions for annual tax review meeting:

- ☐ Have any changes in the tax law occurred 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? Can 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 under the Section 116.007 of Texas Trust Code/Treas. Reg. Sec. 1.643(b)-1?
- ☐ Have the tax brackets or the state of residency of the beneficiaries or the trustee 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?

7.
THE TRUST INVESTMENT PROCESS AND STRATEGY

- ☐ Unless the trust says otherwise, the investment standard for trustees in Texas defined by the Texas Trust Code Section 117.003 is that of a “prudent investor."
- ☐ The duty is process-based (was the decision reasonable at the time), not outcome-based.
- ☐ What are the goals of the trust?
- ☐ Does the trust have any specific investment guidelines?
- ☐ 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? Diversification, while an important concept, is not required if the purposes of the trust are better served without diversifying, Texas Trust Code, Section 117.005.
- ☐ 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? <u>Are the liquid funds invested</u>?
- ☐ If the trust has substantial unrealized capital gains, is there a strategy to manage these?
- ☐ Have the tax impacts of the investment strategy on the trust and the beneficiaries (through their distributions) been considered? Do some assets return principal and income or need specialized accounting like MLPs?
- ☐ If hedge funds or alternative investments are used, have their net-after tax returns been evaluated considering the 2018 changes in the tax law. Note: investment management fees generally are no longer deductible, IRC Sec. 67(g).
- ☐ Are there unusual risks to any assets? Have steps been taken to mitigate?

CREATING THE INVESTMENT PROCESS AND STRATEGY (continued)

- ☐ Are there assets with an expiration date such as copyrights, licenses, or commercial leases?
- ☐ What is the long-term investment goal of the account (growth, growth with income, balanced, income with growth, income)?
- ☐ Carefully consider the mix of risk assets and non-risk assets - stocks & real estate, bonds, and money market funds (Modern Portfolio Theory).
- ☐ 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 a beneficiary been considered (Texas Uniform Prudent Investor Act, Section 117.004)?
- ☐ When/how or under what circumstances will the asset allocation be rebalanced?
- ☐ As the trustee, do you have sufficient experience to manage the trust assets or do you need to hire advisors?
- ☐ Under the Texas Trust Code, a trustee may delegate investment responsibility. See Section 117.011 for the process and qualifications.
- ☐ Have you researched the investment 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?
- ☐ How often will performance be evaluated and what are the benchmarks for each asset type and the portfolio as a whole? Specifically, the total return over relevant time periods (quarter and year-end), total return breakdown and attribution, comparisons to portfolio benchmarks, and risk-adjusted return comparisons over relevant time periods (if available).
- ☐ 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.

CREATING THE INVESTMENT PROCESS AND STRATEGY (continued)

- [ ] 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 and do this when the account is step up!

- [ ] Have the goals of the trust, the time horizon, the risk tolerance, the investment objective, the asset allocation, distribution and liquidity needs, tax considerations, any unique circumstances, and how performance is evaluated been documented in an Investment Policy Statement?

- [ ] Foundations, Pension Plans, and the Endowment Funds of charitable organizations almost always have Investment Policy Statements. Similarly, trustees of family trusts (which may be larger than these non-profits) should have Investment Policy Statements.

- [ ] With defined contribution plans, i.e., 401(k), recently there has been a significant increase in litigation regarding trustees who failed to do reasonable due diligence in negotiating investment management fees and reviewing manager performance. While the platforms and beneficiaries are different, this may indicate a coming trend and trustees should be careful in documenting their due diligence in these areas.

8.

REVIEWING A TRUST SECURITIES PORTFOLIO

- [ ] What are the long-term investment goals of the trust?
- [ ] 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?
- [ ] Does the investment policy statement include the goals of the trust, the time horizon, the risk tolerance, the investment objective (asset allocation), distribution and liquidity needs, tax considerations, and how performance is to be evaluated?
- [ ] Where are the trust assets held? Does the trust have “direct" ownership?
- [ ] 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/
- [ ] If the advisor manages less than $100 million, check the state's site.
- [ ] Ask the advisor if any arbitrated claims were removed from their FINRA/SEC/State report.

9.

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, 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 taxable 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?

DISCRETIONARY DISTRIBUTIONS (continued)

- ☐ Will this distribution be to the beneficiary or paid to someone for his/her benefit?
- ☐ Is the distribution from income or principal?
- ☐ Is this distribution under a "may" or "shall" standard?
- ☐ Distributions from the principal will impact future income and growth of the trust and may incur capital gains taxes for the trust.
- ☐ For this beneficiary, what are the distributions year to date, and for the last calendar year?
- ☐ 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 or other issues, consider True Link, www.truelinkfinancial.com, a prepaid debit card that controls spending under set terms - how much, where, when, and type (food, gas, clothes, pharmacy, etc.) and blocks other businesses (bars, etc.). Note: Walmart, Target, grocery stores, and some pharmacies, depending on the state, sell beer, wine, and liquor.
- ☐ Is this distribution from an exempt or non-exempt generation-skipping trust? Will the distribution cause a generation-skipping tax to be due?
- ☐ A distribution standard such as "reasonable health, education, maintenance, and support," may be modified by any number of parameters. These can be in accordance with the beneficiary's standard of living, with reference to the beneficiary's other resources (the trust may require the trustee to determine these - beneficiary's assets and liabilities, employment income and benefits, government benefits, or support obligations), and whether those other resources might have to be exhausted first.
- ☐ 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.

10.

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 <u>and to build trust.</u>

- [ ] If possible, have a face to face meeting. With multiple, geographically dispersed beneficiaries, consider using WebEx, Zoom, Skype, or other technology. Larger law and CPA firms may have the technology in their conference rooms for a better experience for these meetings.

- [ ] 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.

- [ ] For younger or financially unaware beneficiaries, provide periodic financial education (outsource if necessary, as an expense to the trust).

MEETING THE BENEFICIARIES (continued)

- [ ] 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 the Trust Code does 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).

11.

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 launchpad 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, outsourcing as necessary as an expense of the trust.
- ☐ Consider using www.greenlightcard.com as an app/bank account for younger children in learning to spend, save, and donate.
- ☐ Sharing information about family wealth creates trust.
- ☐ Talk about the meaning of inheritance (James Hughes et al., The Cycle of the Gift, 2013).
- ☐ 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.

12.

TRUST ACCOUNTING REQUIREMENTS

Texas Trust Code (Sections 113.151 and 113.152), requires that, if requested by a beneficiary in a written statement, the trustee must provide within 90 days of the request, but no more than once every twelve months, an accounting showing:

- ☐ Listing of all property administered with an adequate description of each asset;
- ☐ All known liabilities owed by the trust;
- ☐ Listing of all property that has come into the Trust not previously listed;
- ☐ Receipts (income), disbursements, transactions regarding the trust property (including their source and nature) since the last accounting;
- ☐ If necessary, show principal and income separately;
- ☐ Adjustments, if necessary, to principal and income for oil & gas, real estate, and partnerships (depletion and depreciation);
- ☐ Reconciliation of the above assets & liabilities, receipts, and disbursements in the period, and assets and liabilities at the end of the period; and
- ☐ Cash balance on hand and name and location of the depository where held.

Other items required – not in Trust Code

- ☐ <u>Texas's common law of disclosure is much broader than the Trust Code; those requirements should be reviewed with the attorney</u>. A trustee is under a continuing duty to share with a beneficiary all material matters of the administration of the trust. and should not wait to disclose these until the beneficiary asks for an accounting.
- ☐ Material matters to be disclosed may include hiring/firing agents with an important responsibility, significant changes in investment strategy, non-routine purchases/sales of major assets, and litigation updates.
- ☐ 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.

TRUST ACCOUNTING REQUIREMENTS (continued)

- ☐ Accountings for minors should be sent to their parent(s) or guardian.

Other considerations

- ☐ CPAs often provide a "compilation" which is somewhat like an accounting. Be sure fair market values are used for the assets in 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! Depending on the size of the trust and the relative expense, consider using a custodian who can provide trust accounting and who can provide "special reports" when the need arises.
- ☐ 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 held for safekeeping.
- ☐ Confirm that taxes have been paid.
- ☐ In more significant trust/family office situations, be sure internal controls are considered.
- ☐ Have the attorney for the trust review the accounting before it is provided to the beneficiaries.
- ☐ Depending on the size and complexity of the trust, a written summary outlining significant events for the year and a plan for the following year.
- ☐ If an accounting is not provided, the statute of limitations on beneficiaries' claims (generally four years in Texas, absent fraud) does not start to run until the beneficiaries receive the accounting and other material information relevant to the trust.

13.

TRUSTEE RISK MANAGEMENT

Risks, known and unknown, always exist. New trustees generally do not appreciate their potential liability. Litigation is expensive 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.
- [ ] Communicate, communicate, communicate.
- [ ] 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.
- [ ] If the cost of an audit (expensive) is justified by the nature and extent of the trustee's transactions and the value of the trust's assets, consider engaging a CPA to audit the trustee's financials periodically. CPAs can often help a trustee become aware of deficiencies in internal control or weaknesses in financial systems and offer suggestions for improvement.
- [ ] 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 (Texas Trust Code Section 114.005). Especially in matters of importance, the beneficiary should be represented by their legal counsel.
- [ ] Texas Trust Code Section 113.081 allows a court to accept a trustee's resignation and discharge the trustee from the trust on terms necessary to protect the rights of interested parties. Courts almost always will require an accounting.

TRUSTEE RISK MANAGEMENT (continued)

- ☐ Indemnities from beneficiaries are only as good as their financial condition.
- ☐ If the trust agreement is in the drafting stage, ask the grantor of the trust to add language exonerating the trustee from liability (other than for a breach of trust committed in bad faith, intentionally or with reckless indifference to the interest of a beneficiary, or for any profit derived by the trustee from a breach of trust which cannot be waived, Texas Trust Code Section 114.007). Most states have similar exclusions for willful neglect or gross negligence.
- ☐ Consider using Certifications of Trust to avoid disclosure of confidential trust terms to third parties (Texas Trust Code Sec. 114.086).

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 the 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 or 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

ADDENDUM I Successor Trustee

- [ ] Why did the previous trustee resign — death or health reasons, beneficiaries were too demanding or requested resignation, or was there litigation?
- [ ] Read the trust!
- [ ] Does the trust require a review (or not) of the prior trustee's acts? Unless provided for in the trust or releases from all vested beneficiaries have been received, the successor trustee has a responsibility to review on a reasonable basis the acts of the prior trustee.
- [ ] If the document does not relieve that responsibility or if the beneficiaries will not provide a release, consider declining to serve unless there is a judicial accounting of the acts of the prior trustee.
- [ ] Original Trust, Amendments, Court Decrees, Family Settlement Agreements in the file? Are prior trustee resignations and successor appointments in the file?
- [ ] Review the previous checklists, as though this was a new trust.
- [ ] Are federal estate, generation-skipping, gift, and income tax returns in the files.
- [ ] Have you received the income tax returns and statements for the trust for the last three and four years, respectively?
- [ ] History of trust
- [ ] Do any of the beneficiaries have substance abuse or other behavioral issues?
- [ ] Where are the files of the trust, including any attorney's opinions, decisions regarding investments, and distributions?
- [ ] If this was a "Crummey" life insurance trust or an annual exclusion gift trust, are the past annual notice letters and gift tax returns in the file.
- [ ] Does the trust have investment and distribution policies?
- [ ] Have any non-liquid investments recently been independently valued? Is the cost basis available? Is there a plan to hold or sell?
- [ ] Did the beneficiaries get regular statements or accountings?
- [ ] Has a meeting with each beneficiary or beneficiaries collectively been scheduled?

SUCCESSOR TRUSTEE (continued)

- ☐ Is the trust a party to any partnerships or shareholder agreements and do they require attention or notice to make the transition?

DAVE FOLZ

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Business Practice: Dave coaches trustees with respect to their trustee duties and responsibilities, including meetings with beneficiaries, investment reviews, trust audits, discretionary distributions, accountings, and reasonable compensation.

Education:
1986 Southwestern Graduate School of Banking-Trust with Distinction
1982 John Marshall Law School – LL.M. (Tax), Chicago, IL
1973 Georgetown University Law Center– J.D., Washington, D.C.
1970 University of Dayton – B.A.

Career History:

Trust Counselor LLC – Consultant to Trustees, 2015 to present

Texas Capital Bank - Executive Vice President, Chief Fiduciary Officer, Wealth Management and Trust Services, 1999 – 2014

Comerica Bank-Texas – Manager, Trust Services in Texas, 1993 – 1999, acquired NorthPark National Bank (founded its trust and investment services department, 1987-1993)

InterFirst Bank Dallas – Manager, Personal Financial Consulting Services Department, 1980-1987

Continental Illinois National Bank, 2nd Vice President, Trust, 1973-1980

Articles:
TRUSTS AND ESTATES – January-February 1986 "IRA Rollovers"
ALI-ABA, 1986 Cassette tape on "IRA Rollovers"
TEXAS LAWYER – June 16, 2001 "Play the Investment Game to Win"
Master's Thesis for LL.M. "IRA ROLLOVERS"

Books: **ROLLOVER STRATEGIES: TAX AND FINANCIAL PLANNING FOR LUMP SUM DISTRIBUTIONS FROM QUALIFIED PLANS,** 1986, AMERICAN INSTITUTE OF CPAs

Media Resource: Quoted and resource, Dallas Morning News (Scott Burns and Pamela Yip), San Antonio Express, Fort Worth Business Press, American Banker, KVUE Austin (TV), The Future of the Financial Advisory Business (Mark Hurley, author)

Professional: AV Preeminent by Martindale Hubbell

Professional Presentations:

Dallas, North Texas, Fort Bend, St. Louis, Hill Country, South Plains, and Waco Estate Planning Councils, and the Dallas Bar Association Employee Benefits and Trust Estate and Probate Sections on "IRA Rollover Planning," 1986-2011.

Texas Capital Bank, Texas Uniform Prudent Investor Act for Professionals, 2004; SunGard Users Annual Conference "Investments: Best Practices," 2006; Office of the Comptroller of the Currency, Southern Region "Investment Management in the New Millennium: Bank Trust Departments," 2011; Collin County Bar Association and the Texas Bankers Advanced Trust Forum on "Directed Trusts," 2016;

Collin County Bar Estate Planning/Probate Section, "Trustee Boot Camp," 2018; University of North Texas, MBA Program, Special Problems in Taxation, Guest Lecturer (2018 & 2019). Texas based law, CPA, and financial planning firms, "Trustee Boot Camp," 2018 & 2019. "Checklists for Individuals Serving as Trustees," TexasBarCLE, Estate Planning and Probate Drafting, October 24, 2019." Checklists for the New Trustee, Dallas Bar Association, Probate, Trusts, and Estates Section, November 26, 2019.

Professional Associations:

Dallas County Bar Association, Probate, Trusts, and Estates Section
Dallas Estate Planning Council, Past President 2011-2012
DFW Institutional Investment Forum
Illinois State Bar, retired
Independent Trustee Alliance, Board
North Texas Estate Planning Council
Texas Bankers Association, Trust and Financial Services Division, Governmental Relations Committee (2003-2015)

Community Associations:

Metropolitan YMCA of Dallas, Board
Metropolitan YMCA of Dallas Foundation, Chair
Parkland Health and Hospital System, Chair, Investment Committee
Preston Center Rotary Club
Preston Center Rotary Club Foundation, Secretary
Theodore Roosevelt Association, Exec. Comm., and Chair, Invt. Comm.