Report #16 (Thursday, Cont'd)

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

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This Report contains coverage of the Thursday Risk Management general session and Uniform Trust Code special session.

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Risk Management for Trustees: Happy Beneficiaries, Equal Empty Courtrooms Thursday Morning 1/13/05
Presenter: William C. Weinsheimer Esq.

Reporter: Eugene Zuspann Esq.

NOTE: This report supplements Gene's report on the special session for this subject that was published in Report 13.

Why is there a need for risk management?
1. There has been an explosion in the number and complexity of Fiduciary litigation cases 2. Most large firms and boutiques now have an estate and trust litigator 3. More money for the beneficiaries to fight for as death taxes go away 4. Baby boomers are more litigious 5. The Heirs website has materials on suing a trustee

Risk avoidance begins with the pre-acceptance of procedure - the screening process
Analyze the documents, the trust assets and the beneficiaries. Avoid trusts with high risk. Analyze profitability and avoid those trusts that do not meet your standards. Review prior account activity to try and determine if problems exist. If there is a prior trustee, why is the prior trustee no longer serving? If it due to litigation problems with the beneficiaries, determine whether this is a continuing problem.

The bottom line: When in doubt - decline!

Trustees often get sued because they fail to understand their duties as a trustee. The trustee must understand the terms of the trust and administer the trust by its terms. ACTEC is in the process of providing a document for trustees summarizing the trustee's duties that should be published this year. Look for unusual provisions in the trust document. The main message for clients acting as trustees is that they must "dot the i's and cross the t's."

The trustee must understand the duty to furnish information and communicate to beneficiaries. Periodic reports are helpful. Find out what the beneficiaries like. Know what your state law requires.

The trustee has a duty of loyalty and the duty to avoid conflicts of interest. The document may permit conflicts but explain those conflicts to the beneficiaries at the outset. Disclose, disclose, disclose.

The trustee has a duty of impartiality. This does not require treating the beneficiaries equally - treat them impartially. If the instrument directs that one beneficiary will be favored, understand and communicate that to the beneficiaries so they understand why certain actions are taken.

Handling trust investments (pg 18) The prudent investor act is enacted in 43 states. In some states, it was not clear whether this rule created an absolute duty to diversify in all circumstances. The emphasis is on process and procedure. The trustee must act upon the total portfolio. The law in this area is now to review the performance of the total portfolio - a total return review rather than focusing on separate assets. The Prudent Investor Rule is a test of conduct and not of resulting performance.

Diversification - Carefully look at the situation in the trust and document your decision. There is no defined set of asset categories that the trustee must consider. Diversification does not require the trustee to have some investments in land, some in Oil and gas, etc. There must not be a concentration of a class of assets. Set rules for defining and dealing with a concentration. If the trust has a concentration, you may not want to take the trust in the first place. If you are trustee, get consents or releases from the beneficiaries and possibly obtain court direction. Pg 21 contains a list of key factors to be used in formulating an investment program and document your decision. Some of these key factors are size and makeup of the portfolio, needs of the beneficiaries, liquidity and distribution requirements and the purposes and duration of the trust.

If the trustee is not a qualified investment advisor, the trustee should consider delegation of the investment functions. Even for the corporate trustee, delegation is prudent when the trust contains assets which are outside of the trustee’s investment experience.

Unitrust conversion approach. Unitrusts came into being because of modern portfolio theory and total return concepts. Again, the trustee must set rules for defining and dealing with a concentration of assets. The same concepts are relevant to trustees with a power to adjust. State statutes should be analyzed to determine the obligations, duties and liabilities of the trust in exercising the power to adjust or to operate as a unitrust. The governing instrument should also give the trustee protection. The UPAIA provides trustees with significant protection for liability.
Unless it is evident to a trustee that a particular trust is a candidate for conversion, or unless a beneficiary has requested conversion, the trustee should take no action.

If the trust is an income trust with invasion provisions, it is best not to convert to a unitrust. He feels the same result can be obtained under §103 and §104 of the UPAIA. The trustee may wish to obtain the consent of the beneficiaries. He pointed out Jonathan Blattmachr’s comments on Monday suggesting that a trust is much more flexible under the §643 regs if it is not a unitrust.

Delegation to advisors other than investment advisors.
1. UTC 807 provides much flexibility to delegate.
2. R 3rd Trusts states that historically you could not delegate administrative acts without explicit authorization in the trust instrument. R 3rd changes this.
3. The trustee should delegate whenever there are assets in the trust in which the trustee does not have expertise. Some examples are real estate, oil and gas investments, closely held bus interests and intellectual property.

If you are going to delegate, do not act blindly. You must supervise and monitor what is happening, get reports back from the agent, and act if something is wrong.

The trustee should be able to delegate to the co-trustee. You must check the state statutes. Ill does not have a power to delegate to the co-trustee. You also need to check the trust instrument. If there is no power, or if the instrument prohibits delegation, there is joint and several liability.

In discretionary trusts, review the scope of the trustee's discretion with the beneficiaries, explain the scope of standards, explain the scope of broader standards (general welfare and best interests), and, if the trust requires the trustee consider other resources of the beneficiaries, obtain such information.

Determine the language under the document to determine the method of making distributions. Determine priorities. Establish a format for gathering financial and family data from the beneficiaries which will be used to evaluate a requires for a discretionary distribution and give the beneficiaries advance warning that this data will be required before the trustee can exercise discretion. If there is full discretion, review state law and the instrument to determine what still must be done to advise the beneficiary. Make sure that you have sound procedures. Explain the rules of engagement to the beneficiaries. Document your decisions, pro and con.

In general, an attorney can act as trustee for the client, but they must advise the client of the potential conflict, and maybe advise the client to see other counsel to advise on the decision.

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Hot Topics on the Uniform Trust Code
Thursday Afternoon, 1/13/05
Presenters:
Prof. David English (DE)
Prof. Alan Newman (AN)
Suzanne Brown Walsh Esq. (SW)
Richard Davis Esq. (RD)

Reporter: Eugene Zuspann Esq.

DE Started with an overview of the code.

The UTC is the first effort to codify the law of trusts. Together with the UPIA, the UPAIA, this is close to a comprehensive body of law.

There are 3 areas in which people have significant concerns 1. Notice and the ability to waive by the settlor 2. estate tax (modification or termination of trusts by the beneficiaries) 3. creditor claims

The panel spent some time summarizing the law from the states where they are located - Missouri, Ohio and Connecticut.

Ohio made several changes to Section 504 on creditor rights. These include the addition of a discretionary trust with no standards - the trustee has sole and absolute discretion and a beneficiary cannot be the trustee.

DE discussed amendments made to the UTC last summer. There included making §105(b)(8) and (9) optional (allowing a settlor to waive the obligation to report), adding several alternatives to §411 (the modification and termination section that has caused 2036 and 2038 concerns) and changes to the creditor rights article.

The most changed provisions in the code involve the required reporting to the beneficiaries. Of 10 states that have passed the UTC, 4 have modified the statute and D.C. has put in a trust protector concept. Missouri allows waiver of notice to remainder beneficiaries. There is no consistency on the notice issue. This is a significant issue in all states.

DE discussed 411(a) - the ability to modify or terminate a trust, and the proposed changes to the statute. Almost all states now allow modification or termination in some form. This is either by statute or case law. Some states require court approval and some do not. The choices in 411(a) include adding court approval, making 411(a) prospective only or eliminating 411(a) altogether and relying on existing state law.

AN addressed the concerns raised by people worried about an expansion of creditor rights in trusts created by third parties, including spendthrift clauses and discretionary and support trusts. The materials contain a paper he has prepared analyzing these issues.

Further amendments are being considered by the ULC to Article 5 (creditor rights). The committee is looking at the definition of mandatory distribution. §501 will only apply if there is no spendthrift provision. It may enlarge creditors rights in a discretionary trust if the trust instrument does not include a spendthrift clause.

SW discussed the Connecticut changes and the removal of a trustee in §706.

Under §504, it does not matter whether the trust is a discretionary trust or a support trust.

RD spent time discussing special needs trusts (SNTs) and the creditor issues raised that could concern those trusts. There is an article posted on the web at www.oh-elderlaw.com on SNTs.
He feels:
1. SNTs do not need creditor protection to work. The government is not a creditor with respect to benefits paid. Generally, estate recovery only applies to probate assets.
2. Can the existence of an SNT be used to deny benefits?
a. If the trust is pre-1993 and a self settled trust - no. This was changed by OBRA in 1993. Now I understand the answer to be yes.
b. A 3rd party trust cannot be used to deny benefits if properly drawn.
3. SNTs are not countable assets.
4. SNTs are discretionary. Therefore, the beneficiary does not have the right to compel payment.
5. Distributions from SNTs are never in the hands of the beneficiary.

There has been concern about the Kreitzer (??) decision in Ohio. The trust in the case is distinguishable because it did not contain a spendthrift clause and did contain a support standard.

§814(a) does not change this result if properly drafted.

Our on-site local reporters who are present in Miami this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Shelly Merritt Esq., a solo practitioner in Boulder, Colorado, Connie T. Eyster Esq. of Hutchinson, Black & Cook LLC in Boulder, Colorado, Jason Havens Esq. of Havens & Miller PLLC in Dustin, Florida, Bruce Stone of Goldman, Felcoski & Stone, PA of Coral Gables, Florida, Herbert L. Braverman Esq. of Walter & Haverfield LLP in Cleveland, Ohio, and Jeffry L. Weiler of Benesch, Friedlander, Coplan & Aronoff LLP of Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado who is the Chief

Moderator of the ABA-PTL List.

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