BALLENTINE PARTNERS

Estate Planning

Estate Planning Questions and Issues to Ponder[1]

BALLENTINE PARTNERS | ROY BALLENTINE, ChFC, CFP®

This article explores some key estate planning issues that arise in nearly every discussion about estate planning. If couples or individuals arrive in their attorney's office having already considered these issues, estate planning discussions will go more smoothly and couples will feel more confident in their decisions.

Because the concepts discussed in this article are interrelated, you may wish to give it a quick read from start to finish, and then return to the beginning to study each section.

This article has two sections. Section 1 addresses basic concepts. Section 2 (beginning on page 4) provides guidance about some of the key decisions you will need to make.

SECTION 1: Estate Planning Concepts

1. What documents are required for a complete estate plan?

- ***Your will*** – contains instructions for transferring any assets you have not already placed in trust by the time of your death, as well as various tax and other technical provisions. It also appoints your executor(trix) or personal representative for the administration of your estate. You can amend your will during your lifetime as many times as you wish.
- ***Trust document*** – for most wealthy families, one or more trust documents are the key documents that contain instructions for the disposition of assets. The most common type of trust is a revocable trust, also known as a living trust.
- ***Assignment of property to revocable trust*** – if you wish your estate to avoid probate as much as it is possible to do so, then your assets must be assigned to your trusts during your lifetime.
- ***Living will*** – contains instructions for your healthcare when death is judged by your personal physician to be imminent.
- ***Healthcare proxy*** (also called a Healthcare Power of Attorney) – contains instructions for your healthcare when you are incapacitated and therefore cannot make your own decisions but you are expected to recover.
- ***Durable Power of Attorney*** – empowers another individual to exercise full control over your assets during your lifetime; most likely to be

[1] Ballentine Partners does not give legal advice. The paragraphs that appear in quotes are intended to present concepts for solving various practical problems. We have tried to present the proposed solutions in plain English. If you are interested in any of the concepts, your attorney should be able to prepare them in proper legal form.

used if you are unconscious or otherwise incapacitated.

- Depending upon your situation, you may also need a life insurance trust, a buy-sell agreement for your business interests, or various other documents.

2. What is probate?

Probate is a legal process that takes place after someone dies and includes:

- proving in court that a deceased person's will is valid (usually a routine matter);
- identifying and inventorying the deceased person's property;
- having the property appraised;
- paying debts and taxes; and
- distributing the remaining property as the will directs or according to state law if there is no will.

Typically, probate involves paperwork and court appearances by lawyers. The lawyers and court fees are paid from estate property which would otherwise go to the people who inherit the deceased person's property.

Most wealthy families seek to minimize the amount of assets that must pass through probate. Probate is a public process. Anyone who cares to investigate an estate can access the records of the county's probate office and obtain copies of documents, including estate inventories and a copy of the decedent's will.

3. What is ancillary probate?

Ancillary probate is a probate procedure in a legal jurisdiction that is not the decedent's legal domicile. For example, if a decedent's domicile is Connecticut, and the decedent owns real property in New Hampshire, then the decedent's estate will need to engage in a separate probate proceeding in New Hampshire with respect to the New Hampshire real estate.

Ancillary probate may prove to be expensive and time-consuming, depending upon the probate requirements of a particular jurisdiction. this is particularly the case when assets are located in a different country which may have a completely different legal system than the jurisdiction in which the decedent's will was written. For example, US law is based on British common law whereas some European law is based on the Napoleonic Code.

Ancillary probate can be easily avoided through the use of revocable trusts, limited liability companies and other ownership structures.

4. What role does my will play in my estate plan?

Your will transfers to your heirs the assets of which you are the sole owner. It also specifies how your taxes and remaining debts will be paid by your estate.

Notice that your will governs only property of which you are the sole owner at the time of your death. Jointly owned assets automatically pass outside of probate to the surviving owner. Other assets, such as life insurance and retirement accounts, usually pass via their beneficiary designations to one or more individuals outside of probate.

Your will may also create one or more trusts for the benefit of your heirs and then transfer assets to those trusts. A trust created under a will is called a "testamentary trust." However, it is generally preferable for a wealthy family to create trusts under a separate document, called a "revocable trust" or "living trust" (those terms are interchangeable), rather than creating trusts under a will.

Your will also appoints your executor(trix) or personal representative; those terms are interchangeable. Your executor is responsible for probating your estate, as previously described.

5. What is a trust?

A trust is a private contract between the donor (also sometimes referred to as a "settlor" or "grantor" – all three terms are interchangeable) and the trustee (s). The donor can write any terms and conditions into the contract that the donor desires, provided the conditions are not illegal. Once the trustee accepts the contract, the conditions are legally binding upon the trustee.

A key purpose of a trust is to separate legal ownership of assets from beneficial ownership. For example, a minor is not permitted to own real estate outright because a minor has no legal capacity to enter into a contract such as a real estate purchase & sale agreement. However, a trust created for the benefit of the minor child can own real estate if the trust document grants the trustee the legal power to enter into contract agreements.

Most trusts have beneficiaries who are entitled to receive distributions from the trust as well as an accounting of the trust's assets and liabilities. The donor specifies the minimum age for a beneficiary to receive distributions, the amount to be distributed, and potentially how distributions must be used.

A trust can be structured to exist for a limited period of time or for perpetuity. Perpetual trusts are very powerful wealth preservation tools for wealthy families in that they can shelter assets from estate taxes for many generations.

6. What is the advantage of creating a trust under a revocable trust document rather than creating trusts under a will?

A revocable trust is created by a document that stands on its own, is completely separate from your will, and is created during your (the donor's) lifetime. Testamentary trusts can be created only by your will once you die. Revocable trusts offer significant advantages over testamentary trusts.

- A trust created under a revocable trust (also referred to as a "living trust") document can be funded during your lifetime. That is, you can name your trust as the owner of specific assets, such as your home or financial account(s), without the ownership transfer being considered a taxable gift. Your revocable trust can be written so that, during your lifetime, you are both the trustee and the beneficiary of your trust. The trust assets and terms can be altered at any time. This arrangement leaves you in complete control of your assets but it positions your assets so that, when you die, those trust assets will not be required to pass through probate. A testamentary trust can be funded only by a probate proceeding because the trust does not come into existence until the will has been probated.

- As explained below, your Durable Power of Attorney document may or may not be accepted by financial institutions. You can eliminate this problem by transferring all of your assets to your revocable trust while you are healthy. If you become incapacitated after funding your revocable trust, your back-up trustee can take over the management of your assets. Your Durable Power of Attorney does not apply to assets held in your trust. Only the trustee has the authority necessary to manage your assets.

- A revocable trust is private; a trust created under a will (that is, a “testamentary trust”) must be filed with the probate court of the decedent’s domicile and can be accessed by members of the public. Also, the inventory of assets owned by a revocable trust is private, while the inventory of a testamentary trust must be filed each year with the probate court and can be accessed by members of the public.

- A revocable trust does not fall under the continued supervision of the probate court of the decedent’s place of domicile, while a testamentary trust is subject to on-going court supervision. The legal and administrative fees associated with on-going court supervision can be quite burdensome in some jurisdictions.

- After the death of the donor, a trustee can move a trust to a new legal jurisdiction if it was created by a revocable trust rather than a testamentary trust. Wealthy families often choose to move old trusts from their original jurisdictions to new jurisdictions that offer more favorable tax and trust laws to preserve and administer family wealth.

Note that all of the rusts created under a donor’s revocable trust document become irrevocable after the death of the donor.

7. What is an irrevocable trust? How does it compare to a revocable trust?

The donor of a revocable trust retains the right to terminate or amend the trust at any time for any reason during his or her lifetime. A trust that is revocable during the donor’s lifetime becomes irrevocable when the donor dies or becomes legally incapacitated.

An individual may decide to create an irrevocable trust during his or her lifetime. In that case, the donor deliberately gives up the right to terminate or amend the trust. Irrevocable trusts have many uses for wealth transfer planning during the lifetime of a donor.

8. What are the key roles we need to think about with regard to our estate plan?

- ***Personal representative (also referred to as an executor / executrix)*** – Your personal representative is responsible for probating your estate and for the payment of estate taxes and other taxes. Please see the response to question 1 regarding estate planning documents.

- ***Trustee*** – Please see response to question

- ***Trust protector*** – This is an optional role, but one that many wealthy families employ. The role of trust protector is to protect the trust and to preserve the donor’s intent if the need arises. For example, the trust protector may hold the power to remove and replace a single trustee or all of the trustees under certain conditions.

- ***Guardian*** – If you have minor children, the guardian’s role is to care for the children until they reach the age of majority. If you name a married couple as guardians of your children, be sure to specify who will be the guardian if one of them dies or if the couple becomes divorced before or after your death. It is common for the estate plan of a wealthy family to specify that funds from the estate can be used to build an addition onto the home of the guardian or to purchase a larger residence to accommodate the new members of the household. Also, the trustee can be instructed to work with the guardian to provide adequate financial support for the children so they are not a financial burden to the guardian.

- ***Attorney-in-fact*** – The person you appoint as your attorney-in -fact under your Durable Power of Attorney (DPOA) document has the power to buy, sell, and manage all of your assets and liabilities. This person should be someone whom you trust and who has the knowledge and skill to act on your behalf if you become incapacitated. Your Durable Power of Attorney is active only during your lifetime, and it does not apply to assets held by a trust. If you become incapacitated and you are the trustee of one or more trusts, the successor trustee named in the document will take over management of the trust.

- DPOA's are not as effective today as they have been in the past. Many financial institutions will not accept the DPOA even if it has been executed relatively recently. The institution may require the person granting the Power to appear in person (precisely when he or she is not physically able to do so) or to use the particular institution's POA form rather than the document prepared by your attorney. Current best practice is to contact your financial institutions while you are healthy and use their forms to establish the necessary authority now, while you are still competent and healthy, for others to sign on your behalf.

- ***Health care agent*** – The powers of a health care agent vary from state to state. Also, some medical centers impose their own restrictions on the powers of health care agents. The person you appoint as your health care agent will make healthcare decisions on your behalf if you are unable to make your own decisions. For example, in most states your agent can consent to surgery, refuse to have you placed on life support machines, or request that you be taken off life support. The terms health care agent, health care proxy, health care surrogate, and health care attorney-in-fact mean the same thing.

9. What difficulties might family members encounter when trying to gain access to my medical information to help ensure proper medical treatment for me?

- The Health Insurance Portability and Accountability Act of 1996 ("HIPAA") contains confidentiality provisions that may make it difficult or impossible for family members and/ or key advisors to learn anything about your medical condition unless you have signed a waiver specifically granting access to that information. That document is called a HIPAA Waiver.

- With a HIPAA Waiver, you can authorize your health care providers to share with the person(s) named in the document information about your health care. Hospitals and medical professionals will disclose information only to you directly unless they have your written permission which usually must be witnessed and/or notarized. Neither email nor verbal authorization is acceptable. A faxed or emailed copy of the notarized document usually will be accepted.

- The laws regarding medical waivers vary from state to state. For example, Massachusetts law states that a person named as a health care agent under a health care proxy is entitled to access all medical records (even if he or she does not hold a HIPPA Waiver); the federal HIPAA statute expressly states that it does not override state law. A HIPAA Waiver may be included in a Durable Power of Attorney. That is usually a good idea because it may be necessary for the agents named under those documents to access medical records.

10. What are the duties and responsibilities of a trustee?

Your trustee is responsible for the management of the trust for which the trustee has been appointed by you, the donor. If you create several trusts, each trust can have different trustees, or they can all be the same. A trust may have more than one trustee (who are then called co-trustees). The trust document may require the various trustees to act like a board of trustees (with rules about voting), or each trustee may be assigned a specific set of more limited duties. A trustee is required by law to act in a fiduciary capacity, meaning he or she must manage the trust's assets solely for the benefit of the beneficiaries and in accordance with the terms of the trust.

The trustee role requires three sets of skills:

- ***Investment management*** – investment strategy, asset allocation, risk management, cash flow planning, tax planning, managing investment managers, etc. Make investment decisions, or engage an investment expert and delegate authority to that expert in an appropriate manner.
- ***Trust administration*** – hold legal title to the assets of the trust; keep trust assets separate from the trustees' personal assets; interpret the trust document; monitor compliance with the intent of the grantor; provide trust accounting, tax planning, and tax compliance services; report to trustees and beneficiaries; etc.
- ***Beneficiary relationship management*** – keep in touch with beneficiaries; understand their circumstances and needs; decide when and how trust income or principal should be used or distributed for the benefit of the beneficiaries; balance the needs of current and future beneficiaries; etc.

Some trusts appoint three (or more) different trustees, each of whom is an expert in his or her role. The first two roles, as defined above, are mostly technical. The third role is mostly non-technical. Success in all three roles depends upon maintaining excellent relationships between trustees and beneficiaries, and educating the beneficiaries about their rights, duties, and responsibilities.

Trustees can be held personally liable for their decisions. For example, a trustee who makes an imprudent investment decision can be held liable for investment losses. Thus, some individuals who are asked to serve as trustees may be reluctant to agree.

SECTION 2: Guidance for Key Decisions You Need to Make

1. How much inheritance is enough?

There is no simple answer. The answer will depend upon your attitude about money, your assessment of your child's or other beneficiary's sense of self, their accomplishments so far in life, their financial skills, and your relationship with each of them.

The way you answer the question, "How much is enough?" may be influenced by the way you answer other questions on this list. For example, if you have confidence in your choice of trustee and you have structured trusts that provide asset protection and professional management, you may answer differently than if you are thinking that your children are going to have to learn to manage capital on their own and without the benefits of lifetime asset protection.

Our research into the lives of inheritors who grew up to be successful, productive members of society shows that the transmission of values and a personal code of conduct from one generation to another may be the single most important determinant of success in life. Money all by itself does not cause behavior problems. But, it can amplify behavior or self-esteem problems that already are present. It can also accelerate the outstanding performance of an individual who is already a well-balanced person.

For a discussion of this topic from the perspective of beneficiaries, please see: *Raised Healthy, Wealthy and Wise*, by Coventry Edwards-Pitt. Her book is based on a series of interviews with the offspring of families with whom Ballentine Partners has had longstanding relationships. For an in-depth discussion of this topic by a panel of experts, organized and presented by Ballentine Partners, please see: https://vimeo.com/41425148.

Section 2 question 8 of this document provides a description of a formula clause which can help you to answer the "How much is enough?" question.

2. How should I convey my hopes and expectations about how my children will use money they receive from my estate after my death?

The more information you are able to communicate to your children about your hopes and expectations, the better the outcome is likely to be. Families that fail to communicate about this are much more likely to produce inheritors who suffer from a sense of alienation and guilt on the one hand, or a sense of entitlement on the other hand, with respect to family wealth.

The most successful wealthy families—the ones that produce productive and well-balanced family members in each generation—focus on the transmission of sound values rather than on prescriptive rules regarding the use of wealth. Values are best transmitted by examples of behaviors that are consistent with your verbally expressed values. If the elder generation's behaviors are consistent with their expressed values, that will send a clear signal. If the elder generation's behavior is inconsistent with their expressed values, the effort is likely to fail.

Expressing your hopes and expectations about the use of family wealth is not the same as exercising control over how it is used. Many wealth creators have an aversion to exercising "control from the grave." Merely expressing your values to the next generation leaves those individuals free to make their own decisions. This is very different from writing a set of rules into your estate plan that is legally binding upon your trustees, who are then obligated to enforce those rules upon your beneficiaries.

Here are some additional questions to ponder about this topic:

- What are my values regarding the use of family wealth? Is my behavior congruent with my values?
- If I fail to communicate my hopes and expectations, when, how, and from whom will family members and other inheritors learn about those expectations?
- How much control is appropriate for me to exercise over how inherited assets are used, and by whom they are used?
- If I wish to exercise influence or control over how assets are used, what are my goals? What are my motives? How will my goals and motives be perceived by those who are affected by them?
- What, if any, obligation does the next generation of inheritors have to preserve and grow assets for future generations?
- What discussions should I have with my children about my estate plan? When should I have those discussions?

As soon as your family members are ready to begin learning about family wealth management concepts, we believe that family discussions about the family's values and appropriate uses of money are valuable. This does not mean that you have to reveal your entire financial situation to family members—although that eventually may be a comfortable thing for you to do when your children reach adulthood and are well-established in their own rights.

The key question for you to ponder is: How do you prefer that your family members learn about the important decisions you are making—from you directly during your lifetime or from your attorney after your death? After working with wealthy families for more than 30 years, our experience is that family members would much rather hear the story from you.

More than one discussion is required. In fact, a series of discussions over a period of years seems to work best. Family members then have time to develop their understanding, learn new concepts, and more fully absorb the plan.

3. How should I think about the instructions I incorporate in my trust documents?

Tim Belber, author of The Middle Path, answered the question this way (emphasis added by us):

> "You have to remember that all trusts start with a very simple premise: Someone (the grantor) gives something (assets or the corpus of the trust) to another person (the trustee) to hold for the benefit of a third person (the beneficiary). The questions about establishing any trust are therefore 'How will this be for the benefit of the beneficiaries? And how will it enhance their lives?' If the trust is primarily about asset protection and addressing the parent's agenda it will probably fail when it comes to the beneficiaries.
>
> "A very wise attorney once described a trust as a community that could serve the growth and flourishing of all the beneficiaries. If you draft them thoughtfully you can create opportunities for the trustee to be a mentor and the beneficiaries to "benefit" from their combined life experiences.
>
> "There is one caution I also point out. While trusts offer great benefits, it is important that every family member have a chance to build their own personal balance sheet. For an entrepreneur, the personal balance sheet is his credibility and access to opportunities. I regularly work with families to help the next generation begin building their own balance sheet. From a tax and asset protection perspective taking something out of trust doesn't make sense but from a human capital perspective it matters a lot."[2]

4. What financial management skills do my beneficiaries need to have?

Before we talk about financial skills, we need to mention values again. Children who are taught the value of work and are held accountable for the consequences of their actions seem to acquire sound financial skills much more readily than those who are not taught those things. If your beneficiaries need help to develop a higher level of financial management skill, the time to start working on that is now. We can help.

As each member of the next generation reaches maturity, he or she should be brought into the family wealth management process in an

[2] Reilly, Joe – "Exclusive Interview with Author Tim Belber on Developing Wealthy Families," July 24, 2015, emailed to Ballentine Partners by Joe Reilly.

appropriate way. Here is a partial list of skills they need to acquire:

- Demonstrating a willingness to participate in educational sessions and becoming knowledgeable about financial issues;
- Learning how to manage personally owned assets, including:

    - Investment management;

    - Tax management;

    - Cash flow planning and management;

    - Ownership arrangements;

    - Appropriate use of debt; and

    - Insurance arrangements.

- Understanding the purpose and structure of each trust in which the beneficiary has an interest;
- Becoming knowledgeable about the trustee's roles and responsibilities;
- Meeting with the trustees at least once a year to discuss the beneficiary's personal financial circumstances and goals;
- Providing the trustee with an annual assessment of the trustee's performance in fulfilling his or her roles and responsibilities;
- Learning how to work with a team of professional advisors on trust management and personal financial planning issues;
- Understanding the role of trusts in asset protection planning and the value of that type of planning;
- Developing a general understanding of the investment issues related to trusts, especially the asset allocation and risk management process;
- Developing a general capacity to understand fiduciary accounting;
- Understanding generation-skipping planning and other sophisticated estate planning features of trusts;
- Understanding the tax planning and tax compliance issues related to trusts;
- Understanding the budget for the trust and how and in what amount the trustees and other professionals involved with the trust are compensated; and
- Attending periodic family meetings and accepting ownership for responsibilities that are well-suited to each beneficiary's strengths.

5. Should I leave assets to my heirs outright or in trust?

Many families decide to leave a portion of assets to individual heirs outright and free of trusts, and the remaining portion in trust.

The major factors that should be considered in making the decision about an outright gift vs. a gift in trust are as follows on the following page:

	Method of Gifting	
	Outright and Free of a Trust	**Held in Trust**
Complexity	Simple.	Inherently more complex than a simple gift or bequest.
Cost	Low cost. No on-going fee for trustees, trust accounting, trust tax returns, etc.	Must pay on-going fees for trustees, trust accounting, trust tax returns, etc.
Investment Responsibilities	If beneficiaries are well-trained and astute financial managers, beneficiary has direct ownership and control over assets. Beneficiary is totally responsible for whatever happens next.	A trust requires and investment advisors to exercise expert judgement in making investment decisions, including adequately diversifying trust assets.
Spending Constraints and Rights	Beneficiary's rate of consumption is not constrained by the need to balance the interests of current and future beneficiaries.	Trustees are required to balance the needs of current and future beneficiaries. Distributions to current beneficiaries must take future beneficiaries' needs into account unless the current beneficiary is the sole beneficiary of the trust.
Spending Responsibility	Encourages personal responsibility and accountability. The beneficiary must find and manage his or her own team of advisors.	A trust can also encourage personal responsibility and accountability. The donor names the initial advisors to the trust. The donor also decides what, if any, role the beneficiary will have in naming a replacement trustee and/or other advisors if the need arises.
Creditors	All assets are exposed to the claims of the beneficiary's current and future creditors – including spousal claims in the event of divorce.	Assets and trust income can be protected from the claims of current and future creditors of a beneficiary. (Some states may count trust assets in divorce settlements.)
Estate Taxes—Federal	All assets are exposed to estate tax when the beneficiary dies.	Assets can be exempted from estate tax when a beneficiary dies, if the donor elected to make the trust exempt from estate tax when the donor created the trust.
Estate Taxes—State	All assets are exposed to state income tax in the beneficiary's state of residence.	Assets may escape state income tax if the trust is created under the laws of a state that has no state income tax and trust income is accumulated inside the trust.

6. What value does our family put on asset protection planning?

How important is it to protect your family's assets from the potential claims of your children's spouses, personal injury lawsuits, and business creditors? You have a unique opportunity to provide asset protection for your children's inheritance. The assets' future owners cannot easily provide asset protection for the assets, once they receive them from your estate.

If a trust requires assets to be distributed at a specific time, those assets, upon distribution, will no longer be protected from creditors. The following clause provides no asset protection after age 30:

> "...when each beneficiary attains the age of 30, the trustee shall distribute the remainder of that beneficiary's share."

A lifetime trust can be structured to protect assets for the lifetime of each child while still providing your children with considerable control over the assets. For example, if a beneficiary wishes to purchase a house, the trust can purchase the house and allow the beneficiary to live there rent-free. Or, the trustee could lend the beneficiary money at a very low interest rate to provide an inexpensive alternative to a traditional mortgage. Or, the trustee could distribute principal from the trust so that the beneficiary can purchase the house. If the house is owned by the trust, the value of the house will be completely protected from the beneficiary's creditors. If the trust does not own the house but holds a first mortgage on the property, the house will have substantial protection (but not complete protection). If the beneficiary owns the house, there is no protection.

This is an example of the use of a trust to provide asset protection:

> "The trust shall continue for the lifetime of the beneficiary. The trustee shall exercise discretion to distribute income and principal, or to withhold distributions. The trustee may also use trust assets to purchase a residence for the beneficiary, to make loans to the beneficiary, or for any other purpose that the trustee deems advisable. In deciding whether or not to make distributions, the trustee shall first ascertain that the funds so distributed are not likely to be seized by creditors."

So, on the one hand, you could structure your plan so that all assets are distributed free of trust during your children's lifetimes, or you could require that all assets remain in the trust for the children's lifetimes. In between is a whole range of possibilities that provide at least some asset protection. For example, you could structure a trust so that half the assets are held in a lifetime asset protection trust and the other half is gradually distributed at specific ages.

7. How much should we leave to charity?

There is no simple answer to this question, either. Once your estate has exceeded your lifetime and estate transfer allowances, here is an important rule to keep in mind:

> For every dollar you leave to charity, the charity receives a whole dollar and the government gets nothing in taxes. For every dollar that you leave to an individual, either outright or in trust, you also must give the government a dollar in taxes. Therefore for

[3] The Fidelity Charitable Gift Fund, for example.
[4] The Boston Foundation or the New Hampshire Charitable Fund, for example.
[5] There are many more skills that family members can develop through being involved in charitable giving. We have written a separate article on that topic.

each dollar you leave to charity, the net difference in value passing to your personal beneficiaries is only about 50 cents.

A charitable bequest can be left either directly to specific charities, to a donor advised account[3], to a state or community foundation[4], or to a private charitable foundation. A private foundation is a significant undertaking due to its on-going administrative costs and complexity; it warrants a gift of at least $5 million. Any of the above vehicles allow family members to work together on charitable giving.

A lifetime family charitable account can be a great way to give family members a role in managing family wealth and provide you with a vehicle to each family members about your values. It can also provide a training ground for family members to learn about investing, cash flow planning, tax planning, administration, recordkeeping, due diligence investigations, and measuring results[5] open a donor advised fund with as little as $10,000.

8. Since I don't know how large my estate will be, how can I write instructions to divide my estate between family and charity?

A formula clause can solve this problem. A formula clause can refer to any combination of specific amounts and percentages. Here is an example of a formula clause.

> "If my estate is less than $20 million, I leave my entire estate to my children in equal shares."
>
> "If my estate is $20 million or more, but less than $30 million, then I leave each of my children $10 million, and the balance to charity."
>
> "If my estate is $30 million or more, then I leave each of my children $10 million plus 25% (each) of the estate over $30 million. But, my children's shares shall not exceed $15 million each. I leave the rest of my estate to charity. All of the above dollar amounts will be adjusted for inflation for each year starting with 2013."

A formula clause can also be structured to cap the amount passing to charity, rather than capping the amount passing to individual beneficiaries. For example:

> "If my estate is less than $25 million, I leave it to my children in equal shares (and nothing to charity)."
>
> "If my estate is $20 million or more, then I leave the lesser of 10% of my estate or $5 million to charity, and the balance to my children in equal shares."

9. Whom should I name as trustee?

Different trusts can have different trustees. However, we recommend that the trustees of your various trusts be the same people, as often as possible.

An adult beneficiary can serve as trustee for his or her own trust or for his or her sibling's trust. However, if you want the trust to provide asset protection and/or to be excluded from a beneficiary's taxable estate, then the beneficiary cannot be the sole trustee and cannot participate in decisions about distributions from the trust to himself or herself.

We recommend that any trust that holds substantial assets should have at least one professional trustee. Most of our clients engage a trust and estates attorney for this purpose. Family members, including adult beneficiaries, can serve as co-trustees.

As a general rule, the grantor (you) should not serve as trustee of any irrevocable trust whose assets you intend to keep outside of your taxable estate. There is no problem with your serving as trustee of a revocable trust. In fact, that is recommended.

As explained in response to question 10 in Section 1 regarding the duties of a trustee, it is possible to assign specific tasks to each of several trustees. For example, a trust can appoint:

- An *Administrative Trustee* to deal with administration, tax compliance, and other administrative matters. Usually this role is filled by an attorney or a trust company.
- An *Investment Trustee* to handle investment decisions. This need can also be met through a decision by the other trustees to formally delegate investment authority to an investment advisor who agrees to serve the trust in a fiduciary capacity.
- A *Family Trustee* to manage interactions with family members. This person may be a family friend or a family member who is not a beneficiary of the trust.

Trusts often have multiple trustees and require the individuals serving as trustees to be selected from various classes. For example, a trust created for the benefit of multiple generations of a family might require that:

- One trustee must be an Independent Trustee and shall be an attorney who is not related to any member of the family, and who serves as a professional trustee as a regular and substantial part of his or her professional practice; and
- Each family for whom a separate trust is named under this instrument shall appoint a Family Trustee. The Family Trustee so appointed need not be a member of the appointing family.

10. What other factors should I consider in selecting a trustee?

There are many other factors you should consider.

- What experience does each candidate for the role of trustee bring to the job?
- What trust administration skills are required to manage a trust over multiple decades?
- At what point will it be possible for beneficiaries to serve as co-trustees of their own trusts? Do you wish to permit that?
- Is the person you wish to appoint willing to assume the risks associated with serving as a trustee? A trustee who fails to adequately fulfill his or her fiduciary duties may be personally liable to the beneficiaries for investment losses or other losses due to negligence. A trustee can also be sued personally over decisions to distribute or not distribute money to a beneficiary. Although a court may allow a trustee to use trust assets to defend him or herself, the trustee may be personally liable if the court rules against the trustee.

11. If I am thinking about naming an individual as a trustee, what additional factors do I need to consider?

Naming a family friend, business associate, or some other individual as trustee may be appealing for a number of reasons. However, you should consider the following:

- What qualifications does the individual possess that make him or her a candidate to serve as trustee?

- Does the individual have an adequate understanding of trusts and the role of a trustee?
- Is the individual knowledgeable about the risks and responsibilities associated with serving as a trustee?
- Is the individual prepared to make adequate time available to perform his or her duties? The workload for the trustee who is primarily responsible for managing the relationship with the beneficiaries, their spouses, and other family members may become quite substantial at times.
- Is the individual highly skilled and experienced at working with a team of professional advisors?
- Is the individual sufficiently independent of the grantor to qualify as an "independent" or "disinterested" trustee?
- Does the individual reside in a state that has income tax laws that are friendly (or at least neutral) to the trust? (Some states, such as California, tax all of the income of any trust that names a California resident as trustee even if no beneficiaries reside in California.)
- Is the individual clear of real and potential conflicts of interest, and likely to remain free of conflicts in the future?
- How will you compensate the individual for serving as trustee?

12. What are the provisions for trustee removal and replacement?

The trustees you appoint to manage your revocable trust are not likely to be the trustees who actually serve in that role after your death. Assuming you live to a ripe old age, the people you appoint may be retired or deceased by the time they are called upon to replace you as the trustee of your revocable trust.

If you are creating an irrevocable trust during your lifetime, the trustees you appoint now will probably have resigned and been replaced by the time you die.

Therefore, you should pay close attention to the clauses that govern the removal and replacement of the trustee for all trusts you create. In spite of the importance of these provisions, estate planning professionals tend to regard them as "boiler plate" and pay insufficient attention to them in discussions with donors who are establishing trusts.

Here are the questions you should ask about the removal and replacement of trustees:

- What conditions need to apply before a trustee becomes subject to removal? For example, can a trustee be removed without "cause"? If "cause" is required, how is it defined? Who makes the determination that "cause" exists?
- Who has the power to initiate the removal process? What are the steps in the removal process? Whose approval is required?
- If there is an impasse or deadlock in the removal process, how will it be resolved?
- Who has the power to name a replacement trustee or to appoint an additional trustee?
- What are the selection criteria for the replacement or additional trustee?
- If the appointment of a replacement or additional trustee requires a vote, who is allowed to vote and what are the rules for counting votes?

- What, if any, role will beneficiaries have in the selection of a replacement or additional trustee?
- Is there any limit on the frequency with which a trustee can be removed and replaced?
- Are there any term limits for trustees?
- If the trust breaks the work of trustee into separate roles as described in the response to question 2.9, should the procedures for removal and replacement be the same for all trustees, or not?
- What are the advantages and disadvantages of granting my beneficiaries the power to remove and replace a trustee?

We encourage you to consider giving your adult beneficiaries the power to remove and replace the independent trustee at any time for any reason. Any replacement trustee should be a professional or corporate trustee that meets the requirements described in the answer to question 13 or 14 in Section 2. A trustee who knows he or she can be removed by the adult beneficiaries will have a strong incentive to maintain excellent relationships with the beneficiaries and to be responsive and even-handed. Fee negotiations also will be easier.

If you wish to give your children the power to remove and replace trustees, here is a simple example of one way to structure that power in a single generation trust so that there are appropriate limits on the power to remove and replace the independent trustee:

> "Each trust must have at least two trustees at all times. At least one trustee must be an independent trustee (not a beneficiary, and not related to any beneficiary)."

> "Each child may serve as a trustee of his or her own trust, but shall not vote on matters pertaining to discretionary distributions to himself or herself."

> "The independent trustee must be a registered trust company or an attorney who serves as a professional trustee as a regular and substantial part of his or her professional practice."

Wealthy families often create trusts to last for generations and serve multiple related family units. If you wish to allow family members to serve as trustees, you need to include rules for removing and replacing family trustees.

13. What are the advantages and disadvantages of naming a bank or trust company as trustee?

- Advantages include:

  - Access to professionals who understand trusts, trust accounting, taxation of trusts, etc. and who have all of the information systems necessary to handle administration and reporting.

  - Many trust companies will agree to serve as administrative trustee only, leaving you free to appoint the investment manager of your choice.

  - Some small trust companies may be quite flexible and easy to work with.

  - A simple fee-for-service business arrangement (rather than imposing upon a friend or family member).

- Disadvantages include:

  - High turnover among the trust officers at many companies; impersonal relationship.

  - The decision-making process is usually very opaque.. Decisions are made by a trust committee. Beneficiaries and advisors to family members rarely, if ever, will have an opportunity to interact with the actual decision makers.

  - Most trust companies generate most of their revenue through investment management activities. Trust companies are conflicted on this issue.

- Most of the larger trust companies are affiliated with banks or brokerages that sell proprietary investment and insurance products. Over the years, we have had some heated battles with trustees in our attempts to keep high-fee products out of our clients' trust accounts.

14. What are the advantages and disadvantages of naming an attorney, CPA or other professional as trustee?

If you wish to name a professional as a trustee, we recommend requiring that the universe of individuals considered for the role be restricted to those who serve as a trustee as a regular and substantial part of their professional practice. Examples: a trust and estates attorney or a CPA who specializes in the taxation of trusts.

- Advantages

  - Access to professionals who understand trusts, trust accounting, taxation of trusts, etc.

  - Some law and accounting firms have all of the information systems necessary to handle trust administration and reporting.

  - Many professionals will agree to serve as administrative trustee only, leaving you free to appoint the investment manager of your choice.

  - A professional trustee may be quite flexible and easy to work with.

  - Relationships are usually quite stable; turnover is usually low.

  - A simple fee-for-service business arrangement (rather than imposing upon a friend or family member).

  - The decision-making process is usually transparent if an individual professional is the trustee. If a firm is named as trustee, then decisions may be less transparent because they will be made by a trust committee.

- Disadvantages – The problems we have experienced are due to professionals who were not well-qualified in the first instance, or who retired from practice and are well past their prime but have not resigned their trusteeships.

15. Can I require that the investment management function be kept separate from the role of trustee?

Yes. Most states have adopted modern trust laws that encourage and support the separation of these functions. Separating these functions is also a good way to manage the potential conflicts of interest in the role of trustee, provided that the investment manager is truly independent of the trustee and also is not affiliated with a broker-dealer.

16. What relationship will my beneficiaries have with the trustees?

The quality of this relationship will heavily influence the quality of the results that are achieved by your planning effort. The best time to begin working on this relationship is now. Explain to your children and other beneficiaries what you are doing and why. Explain how you selected the trustees. Introduce your beneficiaries to the trustees and encourage them to engage in a dialogue.

You could also set up a gift trust for each child and fund it with a modest amount of capital. The purpose of this exercise is to allow your children to gain experience working with a trustee and to learn about trusts.

If this process begins under your supervision, you will have an opportunity to learn at the same time that your children are learning. You will have time to adjust your plan, if necessary. The chances of long term success will be materially enhanced.

17. What about leaving assets to my grandchildren and later generations?

From a tax planning perspective, leaving assets to grandchildren allows you to skip estate taxes across generations, no matter how much the capital grows. However, some practical issues arise with this planning technique if the value of assets being left to personal beneficiaries is less than approximately $20 million, or if the number of grandchildren is distributed very unevenly across the branches of the family tree. These issues are complicated and are addressed in a discussion regarding generation-skipping tax planning and how to structure trusts that will last for many generations.

Conclusion

We hope you have found this document helpful. If you have additional questions you think we should add to this list, please feel free to call or email us with your suggestions.

About Roy C. Ballentine, ChFC, CFP®

Roy is the Founder of the firm. Roy dedicates his time to thought leadership, strategic oversight of client engagements, and coaching and training our team members.

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