


Pathways

a trust and estate newsletter from Downey Brand LLP

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Multi-Generational Trusts Offer Benefits & Risks
Keeping the "Family" in Family Business
Can You Compel Arbitration?

ASK AN EXPERT

Who might I name as a successor trustee, other than family or friends?

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Who might I name as a successor trustee, other than family or friends?

Selecting a successor trustee can be difficult. A trustee must have the time and skills necessary to discharge fiduciary duties in a fair manner to the beneficiaries. When you do not have family or friends to act, or they are not the best choice, your basic options are a corporate trustee or a private professional fiduciary.

A corporate trustee is a financial institution's trust department or a trust company. There are several advantages to naming a corporate trustee: (1) corporate trustees do not die or become incapacitated (important for longer term or multi-generational trusts); (2) they have experienced personnel who are familiar with the duties of trustees; (3) they tend to be excellent record keepers; and (4) they offer objectivity and impartiality.

A private professional fiduciary is an individual, licensed in California by the Department of Consumer Affairs, whose profession it is to act as a trustee. He or she brings experience, organizational skills and objectivity to the role of trustee, but may retire, become incapacitated, or die. Some people prefer private fiduciaries because they can get to know the particular person who will be taking on the role of trustee. Private fiduciaries also may serve as agent under an advanced health care directive, which can be a valuable service when individuals do not have friends or family in the area to oversee their medical care if they become unable to do so for themselves.

Corporate and private professional trustees charge varying fees. Although you may be reluctant to pay a fee, it may help ensure that your estate is handled efficiently and smoothly. Also, the use of an outside professional may foster family harmony because one family member will not be picked to serve as trustee over others, and the trustee will not have emotional ties to the estate. You might even consider naming an outside professional to serve as a co-trustee along with a family member.

Your estate planner can make suggestions regarding potential corporate and private professional trustees. You should meet with the candidates, if possible, to find a fit that works for you. Go to www.pfac-pro.org for a list of private fiduciaries in your area.

—Sabrina Schneweis-Coe



Can you compel arbitration?

Binding arbitration is a way to resolve disputes through a private hearing before a neutral third party. Given the cost and delay often associated with resolving disputes through our courts, many parties agree to submit potential or existing disputes to arbitration, and arbitration clauses have become commonplace in a broad variety of contracts.

A creator of a trust reasonably might want to insert an arbitration clause into the trust document to avoid the potential for protracted litigation involving his or her beneficiaries, especially when there is reason to think that they may not get along. Unfortunately, however, it now appears that a simple arbitration clause in a trust instrument is unenforceable in California.

In *Diaz v. Bukey*, which the California Court of Appeal decided on May 10, 2011, a beneficiary filed a petition to remove her sister as trustee of their parents' trust. The trustee sought to compel arbitration of the dispute as the trust document expressly required. The Court of Appeal held that a beneficiary of a trust who did not agree to arbitrate disputes arising under the trust could not be compelled to do so. This is certainly not the result that the parents wanted, assuming they gave the question some thought, when they chose to include the arbitration clause in the document that they signed.

If the Legislature does not revise the California Probate Code in response to *Diaz v. Bukey*, is there a way for a creator of a trust to require beneficiaries to arbitrate disputes? One solution would be to have beneficiaries sign a written consent to arbitrate when the trust document is created or amended. But the creator of the trust may not want to share the document with the beneficiaries or may be unable to obtain their signatures.

—Jeff Galvin



The general information in this newsletter may or may not be appropriate for your particular situation. Before taking any action based on this newsletter, you should consult with your estate planning attorney.

Multi-Generational Trusts Offer Benefits and Risks

Multi-generational trusts are increasingly popular in the context of larger estates. The most common example is a trust that a person establishes for his or her children for their lifetimes, with the trust then continuing on for the grandchildren or maybe even the great grandchildren. A multi-generational trust can be useful for a variety of purposes:

- Preserving assets: Trust assets (whether a closely held business interest, real estate, or a portfolio of publicly-traded securities) can be held together and preserved over time. Sometimes the next generation is not well suited to managing the assets.
- Creditor protection: Assets in an irrevocable trust (as opposed to the typical revocable trust) can provide protection against the beneficiary's creditors. An increasingly common creditor is an ex-spouse in a divorce. Multi-generational trusts are often established with a view toward preventing family assets from being taken in divorces.
- Transfer tax reduction: Some people use multi-generational trusts to avoid gift or estate taxes that would otherwise be imposed as assets pass from generation to generation. If a multi-generational trust is established in an income tax favorable state, the growth in trust principal over the years can be amazing. A very long term multi-generational trust established for this purpose is commonly referred to as a "dynasty trust."



The traditional "rule against perpetuities" generally limits the term of a trust to about 100 years. California retains that rule, but many states have either abolished or greatly relaxed it, even allowing dynasty trusts of even unlimited duration. In our experience, most clients feel that a trust lasting the better part of a century is long enough, particularly given the uncertainty regarding how future generations might be affected by significant "inherited" wealth. Clients who want longer trusts might establish them in states that have abolished or relaxed the rule against perpetuities.

A multi-generational trust is not like the typical "living trust" that may be freely amended or revoked. Instead, trust documents establishing multi-generational trusts typically are irrevocable after the creators of the trust have passed away. California, like most states, has statutes allowing those who establish irrevocable trusts (or in some cases the trust beneficiaries or trustees) to obtain a court order amending the trust document under certain circumstances.

This is commonly done when, for example, a trust beneficiary has special needs or other problems that could not be reasonably anticipated at the time of trust formation.

In order to avoid having to seek court permission to amend an irrevocable trust document, it is possible (and increasingly common) to draft significant flexibility into the document. In many cases the trust

document will allow for the appointment of a special trustee or other agent to carry out certain tasks or even amend the trust document. A catchall term for such a special trustee or agent is a "trust protector." For example, it is possible to name a trust protector, or allow the beneficiaries to appoint a trust protector, to amend the trust document in response to changing laws, to change the trust situs (central place of management) and governing law from one jurisdiction to another, or to make other amendments necessary to have the trust operate efficiently over time.

Multi-generational trusts may create conflict between current income beneficiaries, such as the children, and remainder beneficiaries, such as the grandchildren. The children typically have an interest in maximizing income distributions, and may request a discretionary distribution from principal, while the grandchildren have an interest in principal preservation and growth. Litigation between children and grandchildren is an unpleasant possibility. In drafting the trust document, an estate planner can attempt to reduce the potential for this sort of conflict.

In sum, multi-generational trusts are not desirable for every client, but they can be useful under the right circumstances.

—Sil Reggiardo



Keeping the “Family” in Family Business: The Capitol Region Family Business Center

It is commonly said that nearly all family businesses fail by the third generation. While most mom and pop operations can make it to the next generation, only a select few succeed when ownership is fractionalized and divided among more distant relatives. The biggest threat to the succession of a family business is the failure to plan for the transition of both ownership and management from generation to generation.

The issues that prevent proper planning might touch on every facet of a family’s life, such as strained relationships, communication struggles, retirement and cash flow, separating management and control from ownership, estate planning and taxes, and identifying the family’s continuing mission and legacy. These are tough issues for a boardroom discussion and even more difficult around the family’s holiday dinner table.

Although professional advisors serve an important role in helping family businesses with succession planning, it can be very helpful for families to hear from other families in the community which have dealt with these often non-technical, very emotional issues. Downey Brand is a proud sponsor of the Capitol Region Family Business Center (FBC). The FBC is a non-profit entity which was

founded by prominent family businesses in the Sacramento region, from Modesto to Chico, with the goal of helping family businesses grow and prosper. The main purpose of the FBC is to provide a forum for families to share their stories of success and failure, so that others can learn from their triumphs and disasters.

The FBC hosts events throughout the year for family businesses, bringing in leading experts in their field to discuss both technical and non-technical planning issues imperative to the long term success of family businesses. Their presentations also feature members of family businesses who share their personal experiences with succession planning. In addition, the group hosts frequent “affinity group meetings” for different family members depending upon their generational assignment and whether they are active in the family business.

If you are interested in attending any of these events, please contact me or check the FBC’s website at <http://www.tcrfbc.org>. –Gina Lera



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