

# Pathways

a trust and estate newsletter from Downey Brand LLP

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## It's Not Easy to Be Mom and Dad's Successor Trustee

### ASK AN EXPERT

Does the new tax law allow you to simplify your trust?

My mom died and I am successor trustee. How long will it take me to administer and then close her trust?

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# ASK AN EXPERT



## Does the new tax law allow you to simplify your trust?

Married couples routinely provide in their joint revocable trusts for division of the trust estate at the first death with the deceased spouse's share of the trust estate being held in either one or two irrevocable sub-trusts for the lifetime benefit of the surviving spouse.

This trust structure has enabled spouses to make optimal use of the deceased spouse's estate tax exemption.

The tax act passed in December 2010 has caused us to re-evaluate this routine approach to trust design. The estate tax exemption amount was increased to \$5 million per person (indexed to inflation), and the exemption amount is now "portable" as between spouses, so that any exemption not needed to avoid tax at the first death can be transferred to the surviving spouse.

Clients with total estates less than \$10 million are now asking: "Why do we need this complicated trust structure that requires the surviving spouse to fund and administer more than one trust following the deceased spouse's death? Can't we now just leave everything in one trust that remains amendable and revocable by the surviving spouse?"

It is true that leaving everything in one revocable, amendable trust following the first death is administratively easier for the surviving spouse and leaves him or her with the maximum amount of planning flexibility. However, good reasons remain for placing the deceased spouse's share in a separate trust.

First and foremost, leaving the deceased spouse's share in a separate, irrevocable trust avoids the risk that the surviving spouse will amend the trust so as to disinherit children or others that the deceased spouse wanted to benefit. Second, it is not clear whether the increased exemption amount or the new provision for portability of the estate tax exemption will still exist after 2012. Current law calls for those provisions to "sunset" at the end of 2012 and for the exemption amount to revert to just \$1 million. So long as the future estate tax law remains in limbo, married couples should remain

focused on making optimal use of the deceased spouse's exemption rather than relying on portability to save the day at the surviving spouse's death. — Jim Deeringer

## My mom died and I am successor trustee. How long will it take me to administer and then close her trust?



There is no set timeframe to complete the administration of a trust. The length of time between the death of the settlor and the termination of a trust could be as short as a few weeks or as long as several generations depending on the terms of the trust and other factors, including whether there are estate tax issues or creditor issues, whether court involvement is necessary to marshal assets or interpret trust provisions, and whether the beneficiaries are litigious.

Generally, where the terms of the trust require outright distribution to a few beneficiaries, the administration can be completed within a few months. Some trusts, however, require that the trust assets remain in trust for a beneficiary's lifetime, or until a beneficiary reaches a certain age, in which case the period of administration could last many decades. A dynasty trust requires that the assets be held in trust for generations.

Although trusts are designed to avoid court oversight, court involvement may be necessary, leading to a longer period of administration. For example, it may be necessary to petition the court for clarification of trust terms where there is an ambiguity. Additionally, there may be assets held outside the trust over which the successor trustee has a claim of ownership. This generally occurs when the grantor either failed to fund the trust completely or failed to transfer title of certain assets into the name of the trust. In that case, the court may transfer the assets into the trust, although a summary administration procedure may be available if the assets are of modest value.

The period of administration also could be protracted due to litigation over the validity of the trust or a particular action taken by the successor trustee. For example, heirs of the settlor may dispute the validity of the trust. Additionally, a trust beneficiary may object to successor trustee's accounting or valuation of assets. — Kelly Tiberini

*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.*

# It's Not Easy to Be Mom and Dad's Successor Trustee

Most couples who create trusts choose one or more of their children, or other close relatives or friends, to serve as their successor trustee or trustees. Usually that works out just fine. But the successor trustee's role is unfamiliar to most of us and can be quite difficult.

A typical joint revocable trust is virtually invisible upon creation. As long as Mom and Dad are the settlors (*i.e.*, creators), trustees, and sole current beneficiaries of their trust, there is no practical change in how they manage their financial affairs. They can spend trust assets as they choose and need not account to the trust's beneficiaries.

The situation changes when Mom or Dad dies. The trust document often calls for the decedent's separate property and share of community property to be held in trust to benefit the survivor during her lifetime, with the remainder to the children. The surviving spouse usually must value and segregate the decedent's share of their property and then follow limitations in the trust document with regard to spending those assets.

When conflict erupts, it typically occurs after Mom and Dad are deceased. This is when the successor trustee has taken control of trust administration. Presto! The successor trustee who has a sibling relationship with her brothers and sisters all of a sudden also becomes their fiduciary with the attendant duties of care and loyalty.

While Mom and Dad happily may have allowed their daughter to harvest and sell the walnuts in the orchard, or to live at the ranch house rent-free, her siblings may fault her if she continues that practice after she becomes trustee. What was once acceptable may become self-dealing.

The successor trustee must administer the trust according to the terms of the trust documents and the governing law. Thus, the trustee should read and periodically review the

trust documents to make sure she is acting within their scope. The key is how Mom and Dad articulated their intent in the documents that they signed – successor trustees sometimes stray by acting based on what they believe their parents wanted rather than on what the documents actually say.



Successor trustees also must understand, however, that that law sometimes overrides the trust documents. For example, the documents may on their face excuse the trustee from liability for any error, but the trustee (under the California Probate Code) will still be liable for gross negligence or intentional misconduct. Likewise, even if the trust states that the trustee has unfettered discretion, the law still requires the trustee to act

reasonably.

The successor trustee must manage assets under the Uniform Prudent Investor Act. If Mom and Dad were heavily invested in a favorite stock, the law may require the successor trustee to diversify the trust's assets within a reasonable time after taking over as trustee. Consulting a professional investment advisor may be necessary if the assets will be kept in trust for a while. The advisor can help the trustee craft and implement an investment plan consistent with the purposes, terms and distribution requirements of the trust.

Sometimes the trustee will have discretion to make distributions to beneficiaries for their health, education, maintenance or support. Is it appropriate to make a discretionary distribution to cover the cost of cosmetic surgery? The trustee will need to collect enough information to exercise sound discretion and then preserve a record of that decision.

The successor trustee must keep the beneficiaries reasonably informed regarding trust administration. More specifically, the trustee must provide a detailed accounting

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to beneficiaries at least once a year (though in practice accountings may be less frequent) and must respond to beneficiary requests for information or documents. The trustee likely will need help from an accountant with regard to trust accountings and tax reporting.

Transparency and disclosure help maintain positive relations between trustee and beneficiaries. Also, the three-year statute of limitations for breach of trust claims generally does not start until beneficiaries have received information from the trustee.

Unless the trust says otherwise, a trustee is entitled to charge a reasonable fee for her services. A trustee should keep detailed time records, day by day, of the hours spent and tasks performed. Fees may cause friction with beneficiaries who do not understand the work involved or think the trustee should volunteer. The trustee may ultimately opt to waive her fee, but that is a decision that is best made towards the end of trust administration.

An attorney can play a key role in helping a successor trustee administer a trust, and trustees usually may hire counsel and pay reasonable legal expenses from trust assets. In some situations, however, the prudent trustee may decide to use her own personal funds to seek legal advice. To the extent the trustee uses trust assets to pay for legal or other expenses, the beneficiaries may contest the propriety and/or amount of the expenditures.

In sum, most successor trustees are able to complete trust administration without problems. However, it's not easy to serve as successor trustee, and it can be downright difficult when trust terms or assets are complex, or when there is tension among the beneficiaries. To smooth administration, Mom and Dad might opt to name a third party professional to act as successor trustee, or the family member selected to serve as trustee may choose to step aside in favor of a professional. —Jeff Galvin



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