TULLY RINCKEY PLLC
YOUR LAWYERS FOR LIFE - 1888LAW4LIFE.COM
441 NEW KARNER ROAD
ALBANY, NEW YORK 12205-3884
1-888-LAW4LIFE
FAX: (518) 218-0496
WWW.1888LAW4LIFE.COM
EMAIL: INFO@TULLYLEGAL.COM

TRUSTEE HANDBOOK

RICHARD E. ROWLANDS, ESQ.
Tully Rinckey, PLLC
441 New Karner Road
Albany, New York 12205
(518) 218-7100
(518) 218-0496 fax
rrowlands@tullylegal.com

TABLE OF CONTENTS

FORWARD

The accuracy and applicability of specific issues raised in this Guide, and the possibility that there may be other relevant issues not raised here, should be addressed with an attorney in our office.

As your attorney, I recommend this Guide to you because you are interested in what it means to be a trustee. Perhaps you are considering naming a trustee for your family, or perhaps someone has suggested that you serve as a trustee yourself.

The text of this Guide is a consensus of suggestions and considerations. Reading the text will not equip you to be a trustee; but, instead, it is intended to offer you an appreciation of what it means to be a trustee. For those considering accepting a trusteeship, the goal is not to encourage or discourage but rather to insure that any such decision is made with sufficient information to understand the basic ramifications.

A. GENERAL STATEMENT

While there are many types of trusts, and trusts are used to accomplish a wide variety of objectives, as exemplified in Appendix A here, the essence of a trust is a legally binding arrangement under which a person, as "grantor" appoints another person, as trustee, to hold property in a fiduciary relationship for a third person, the "beneficiary." That is the essential structure, but frequently the arrangement may be for multiple beneficiaries, and sometimes with multiple trustees, and occasionally multiple grantors. The obligations of a trustee are defined by law and by the trust instrument, which may be the Will of someone who has died, or an agreement or other lifetime document, and which spells out the uses to which the property is to be applied. Appointing someone to be trustee implies a confidence in that person and an expectation that he or she will apply the property faithfully and according to the grantor's objectives for the benefit of the beneficiaries and not for the personal benefit of the trustee.

The administration of a trust is governed primarily by state laws, although Federal tax laws and other regulatory provisions also are part of the picture. The required amount of court involvement in the administration, can vary widely and may determine how burdensome the job of trustee can be.

We will begin with an overview of a trustee's ***duties***, some of which may be specified in the governing instrument and some of which may be explicit or implicit in applicable state and federal law. To perform those duties, trustees are given ***powers***, and some of those as well are specified in the governing instrument while others are explicit or implicit in applicable state or federal law. In New York, the statutory trustee powers are contained in the NY Estates, Powers and Trusts Law (Appendices C). Following overviews of those subjects, this Guide will offer practical and administrative points to consider when addressing what it means to be a trustee and points to think of in choosing a trustee or deciding whether to become a trustee.

B. GENERAL DUTIES OF A TRUSTEE

A trustee stands in a special relationship of fiduciary responsibility to the grantor of the trust and to the beneficiaries. In carrying out his or her fiduciary duties, the trustee must be mindful of that unique relationship. The starting point is the trust instrument and its specification of what the trustee is to do to accomplish the purposes for which the trust has been established. For example in the case of the simplest trust disposition, the instrument might state that the trustee is to hold and invest the assets, to pay net income to beneficiary #1 for life and then to distribute the remainder to beneficiary #2. The emphasis on a particular duty may depend on the purpose for which the trust was created. In the rest of this section are general descriptions of basic categories of a trustee's typical duties, prescribed by the trust instrument and governing law.

1. **Duty to Administer Trust by Its Terms**. The trustee is obligated to administer the trust strictly by its terms. The trustee must be guided in all acts by the trust instrument, including any amendments, and unless there is an absence of direction or ambiguity, must be limited by the intent apparent from the face of the trust instrument. Therefore it is critical that the trustee read and understand the entire trust instrument. To the extent the trustee needs guidance in interpreting the terms of the trust, he or she should seek advice from an attorney in our office.

2. **Duty of Skill and Care**. The laws of most states require that a trustee administer the trust with the care, skill, prudence and diligence that a person familiar with the job of serving as a trustee would use in the conduct of the trust's activities to accomplish the purposes of the trust.

3. **Duty to Give Notices**. The trustee must read the trust provisions carefully to determine the circumstances in which he or she is required to give notice to beneficiaries, co-trustees and successor trustees.

4. **Duty to Furnish Information and to Communicate**. The trustee has the duty to keep the beneficiaries informed regarding the trust and its administration. The trustee should provide the beneficiaries with information about the assets of the trust and the trust's investment performance, and should provide each beneficiary with other information about the trustee's acts and the administration of the trust which is relevant to the beneficiary's interest. The trustee also should provide any additional information reasonably requested by the beneficiary.

5. **Duty to account**. The laws of most states require that the trustee periodically provide the current trust beneficiaries with a written accounting of the assets, liabilities, receipts, and disbursements of the trust. The form and frequency of the accounting will vary from state to state, and any depend on the value of the trust and the number and sophistication of the beneficiaries.

6. **Duty Not to Delegate**. Generally, the trustee has a duty not to delegate to others the performance of any acts the trustee can reasonably be expected to perform personally, particularly acts involving the exercise of judgment and discretion. The trustee should keep records documenting the basis for any significant decision. The trustee may employ agents, such as attorneys, accountants and investment advisors, to advise or assist in the performance of administrative duties. The trustee may not, however, blindly follow their advice. Although some states, like New York, specifically authorize the trustee to delegate investment functions to a professional investment advisor, the trustee must still maintain supervisory responsibility. The trust instrument may authorize a trustee to delegate some or all of his or her powers to a co-trustee.

7. **Duty of Loyalty**. The trustee is obligated to administer the trust solely in the interests of the trust beneficiaries. The trustee may not engage in any act that puts his or her personal interests in conflict with those of any of the trust beneficiaries.

8. **Duty to Avoid Conflict of Interest**. The trustee has a duty not to use trust property for his or her personal gain or for any other purpose unconnected with the trust, nor to take part in any transaction in which the trustee has an interest adverse to a beneficiary. In general, the trustee may not use trust assets in any manner that benefits the trustee personally, even if there is no loss to the trust. The trustee should consult with an attorney regarding any proposed transactions which the trustee suspects might violate this rule. Note, however, that the trust instrument may authorize the trustee to engage in a transaction which would normally constitute a prohibited conflict of interest; for example, if the trustee is a beneficiary, or is related to a beneficiary, the trust instrument may authorize the trustee to buy designated assets from the trust.

9. **Duty to Segregate Trust Property**. The trustee has a strict duty not to commingle personal funds or other non-trust assets with the property of the trust. Trust property must be separate at all times from the trustee's personal funds.

10. **Duty of Impartiality**. The trustee has a primary duty to treat the beneficiaries impartially, unless otherwise specifically provided in the trust instrument. That means that the trustee must show impartiality in balancing the interests of lifetime beneficiaries with those of remainder beneficiaries, and in balancing the interests of members of the same class. The trustee must also balance the interests of lifetime and remainder beneficiaries when making investment and discretionary distribution decisions.

11. **Duty to Invest**. The trustee has the duty to invest trust assets in a manner which is appropriate for the particular trust. Unless otherwise required by the trust instrument, the trustee will generally have a duty to diversity investments and determine an appropriate asset allocation program. That duty begins as soon as the initial assets are received by the trustee. The trustee should become familiar with the specific investment directions given in the trust instrument, and also must

know the investment directions and restrictions under governing state law. In those states like New York which have adopted the Prudent Investor Rule, a trustee who is not a professional investor *would be well advised to delegate investment functions to a professional investment advisor*. An overall concept to keep in mind is that a trustee must be prudent in his or her handling of trust investments. This requires that the trustee determine the financial needs and risk tolerance of the beneficiaries in establishing the investment objectives and program for the trust.

12. **Duty to Enforce and Defend Claims**. The trustee has a duty to take reasonable steps to enforce claims on behalf of the trust and to defend the trust against adverse claims. In deciding whether to enforce a claim, or defend the trust against a claim, the trustee should consider the economic realities of the situation. If the costs of enforcing or defending a claim outweigh the potential benefit to the trust, the trustee may be well advised to settle or abandon the claim. A successor trustee may be obliged to examine the acts of a prior trustee to determine if a possible claim exists in favor of the trust.

13. **Duty of Confidentiality**. The trustee should keep the affairs of the trust confidential, unless otherwise required by law. For example, the trustee should not disclose the terms of the trust, the identity and interests of the beneficiaries or the nature of the trust assets to anyone who is not a beneficiary of the trust or who does not need this information to assist in the administration of the trust. In addition, the trustee should keep confidential any personal information he or she has learned about the beneficiaries through serving as trustee.

C. POWERS OF A TRUSTEE

On becoming a trustee one enters a relationship which is governed by rules and bounded by limits. A trustee who thinks of himself or herself as controlling the relationship is far more likely to encounter serious trouble than a trustee who recognizes that the more practical characterization is that of a faithful partner with the grantor and the beneficiaries, in fulfilling the trust's objectives.

This section addresses "administrative powers," which generally enable the trustee to perform his or her duties and to achieve the assigned objectives. The governing instruments for most modern trust relationships contain lists of "powers and authorities," describing such things as types of permissible investments, the manner by which trust property may be bought, held and disposed of, and how discretionary elections and other decisions may be made. Beyond what is in the governing instrument lies a large body of trust law which the trustee must heed.

Although there are risks in generalization, the operating principle in most instances is as follows: (a) if the governing instrument clearly allows an action to be taken, it may be taken if the trustee believes it appropriate and fair to the beneficiary, or (b) if permitted by state law the action may be taken even if the trust instrument lacks sufficient specificity, but (c) if the instrument and state law are silent, the trustee may petition a local probate court or other court having appropriate venue and jurisdiction, for instructions as to the actions to take.

D. INVESTING TRUST ASSETS. State law governs what investments are appropriate for trust assets. The trust instrument can also expand or reduce the limits of state law as to what are appropriate trust investments in a particular trust.

Historically, most trusts have been drafted to require that the trustee distribute income to one beneficiary or several beneficiaries and hold the principal for the remainder beneficiaries or ultimate beneficiaries. In deciding upon investments, then, the trustee owes a duty of impartiality to both sets of beneficiaries; therefore, the job of investing trust assets has been viewed as requiring a balance between income and capital appreciation. For many years, state laws created lists of legal investments for trustees. A trustee was protected from liability for investing in the listed securities.

The late 1950's saw the birth of an approach to investing often called Modern Portfolio Theory. That Theory's premise is that risk can be quantified and that risk and return work together over time. Also, the theory holds that asset allocation, rather than market timing or security selection, is a primary determinant of portfolio performance. Maximizing current return might be inconsistent with maximizing "wealth." Investment professionals now typically concentrate on portfolio design to maximize "total return," without regard to whether particular assets are held for production of interest or dividends or capital gains. The laws governing trust investments have reflected a struggle to accommodate those modern investment theories. National organizations of trust lawyers and law school teachers have designed model laws, including, "Prudent Investor Rule" and "total return" statutes, to enable trustees to employ Modern Portfolio Theory, and new York has adopted those laws.

Investment strategy must also be guided by the purposes of the particular trust. In determining a strategy, the trustee must consider the expected duration of the trust, the needs of the beneficiaries and applicable tax consequences.

Trustees have always been under a duty to diversify trust investments, but the newer laws designed to accommodate Modern Portfolio Theory particularly emphasize the importance of diversification.

E. **DISTRIBUTING TRUST ASSETS**

One of the fundamental duties of a trustee is to make appropriate distributions to designated beneficiaries. While that obligation of the trustee may seem obvious, it is a matter of substantial importance and potential liability to the trustee. That is compounded by the fact that many trust instruments give the trustee broad discretion in the determination of beneficiary distributions, both as to timing and amount. The issues surrounding distributions to the beneficiary are relevant not only during the existence of the trust but also at the termination date when final distributions are required.

1. **Required Distributions during the Existence of the Trust.** Assuming the language of the trust instrument is clear and unambiguous, required distributions to a beneficiary during the existence of the trust are generally obvious to both the trustee and beneficiary; but if the wording of the trust instrument is not clear, or is ambiguous, the trustee may need to seek judicial interpretation. It is common for a trust to contain provisions requiring the distribution to a beneficiary of all net income earned from the trust assets. While the required income distribution may be clearly stated in the trust instrument, it does put considerable importance upon the trustee's proper allocation of receipts between the income and principal of the trust and also upon the selection of appropriate investments. Another common form of required distribution is a specific dollar amount payable on a regular basis to the beneficiary. That dollar amount may be calculated in many difference ways such as a percentage of the current value of the trust assets, as a fixed dollar amount, or as a combination of the two.

2. **Discretionary Distributions during the Existence of the Trust**. It is also common for the terms of the trust instrument to give the trustee certain discretion in making distributions to the beneficiary during the existence of the trust. Those discretionary distributions may be coupled with other required distributions or may be the sole method of making distributions to the beneficiary. The provisions concerning discretionary distributions may vary widely among trust instruments. For example, the trust instrument may provide the trustee with discretion to make distributions to the beneficiary without any guidelines or without any limitations upon the trustee's authority. On the hand, the terms of the trust instrument may provide the trustee with written guidelines within which to exercise the discretionary distribution powers. One typical approach is to provide the trustee with authority to make distributions to the beneficiary to provide for the beneficiary's "health, education, support and maintenance." Even so, such descriptive wording describing the grantor's intentions regarding discretionary distributions (often called "ascertainable standards") will require substantial judgment by the trustee in determining the needs of the beneficiary. The trustee may find it necessary to secure data from the beneficiary to justify the exercise of the discretionary distribution power. The trustee may also find it necessary or appropriate to consider the other resources of the beneficiary before making such discretionary distributions. All of those possibilities may be more specifically provided for in the trust instrument, or it may be that the trustee must rely upon the trustee's own independent judgment and evaluation.

3. **Termination Distributions**. The final distribution which the trustee is required to make is the allocation of assets among the appropriate recipients upon the termination of the trust. It is not unusual for the trustee to seek judicial authority for such termination distributions even though the trustee may have operated the trust independently of court supervision up to that time. Determining the appropriate beneficiaries and their respective distributive shares, and the powers for actual transfer of assets, are all important aspects of final distributions.

4. **Total Return Trusts**. With the acceptance of Modern Portfolio Theory it has become increasingly apparent that traditional principles of allocating receipts between income and principal may cause needless conflicts between the trustee and the beneficiaries. That conflict is most clearly demonstrated in the circumstance of a beneficiary receiving the income for a fixed period of time and the principal being distributed to another beneficiary at the termination of that fixed period. While the beneficiary whose interest relates solely to income distributions will seek to maximize the allocation of receipts to the income account, the beneficiary who is destined eventually to receive the principal will prefer to maximize the allocation of receipts to principal. That divergence of interests can become difficult for the trustee to resolve, because some assets may provide greater income and less principal appreciation while others may provide less income and greater principal appreciation. As a result, there is a developing approach to trust distributions encompassed under the umbrella description of "total return trust." Although that subject is beyond the scope of this *Guide*, it does justify a simple comment. Among the many developments under the "total return trust" approach are statutory changes allowing the trustee to modify the allocation of receipts between income and principal to more properly reflect the interests of the beneficiaries, rather than having to use traditional rules of allocation. Another version of "total return" legislation allows for the conversion of a mandatory payment of net income into an annuity or unitrust interest (typically in the range of 3% to 5% of the prevailing aggregate value of the trust assets). There also are other methods of distribution which are not tied to the traditional income and principal allocation concept. The form and language of those provisions are varied and sometimes complex, and require careful thought and reliance upon qualified legal counsel in their drafting and implementation.

F. RECORD AND ACCOUNTINGS

1. **Overview**. To serve responsibly a trustee *must keep clear trust records* and *provide accountings* to beneficiaries. Records and accountings are management tools that are the basis for critical actions of the trustee including creation of a thoughtful investment policy, selection of asset managers, administration of illiquid assets such as a closely-held business or real estate, strategic income and wealth transfer tax planning, and, of course, beneficiary reporting. A trustee who is unable to account for the trust estate properly will likely have difficulty succeeding in a legal proceeding, and may even be removed or suffer a loss of compensation or be charged with personal financial liability.

2. **General Records of the Trust**. Virtually all trusts hold financial assets, and those assets occasion written records such as bank statements, cancelled checks, brokerage statements and security trade confirmations. Other asset classes such as real estate will also have a routine set of records. Copies of filed tax returns are also a standard part of trust records. All trust records are important for legal and tax purposes and need to be retained din an orderly fashion. Reasonable record keeping is an inherent part of all trustee duties, particularly the duty to account.

Moreover, trust beneficiaries usually have a right to inspect trust records, subject to legal limitations in some cases. *Appendix B* contains a list of typical records that trustees keep.

3. **Records of Trustee Actions**. Trustees often are authorized by the trust instrument to make discretionary decisions. Those are nonrecurring events and need to be documented clearly. For example, a trust instrument may authorize the trustee to distribute trust principal for educational expenses. If the trustee exercises that discretion and makes a payment, the decision should be supported by memorandum or correspondence. Records of trustee actions can be highly formal (a vote of co-trustees on the sale of a business) or informal (the letter by which a beneficiary requested a payment which the trustee made), but some such written support is essential.

4. **Trust Accountings**. The beneficiaries of a trust have a legal right to receive sufficient information about the trust to protect their beneficial interests in the trust. That legal principle is the foundation of the trustee's legal duty to account to the beneficiaries, and provides the basis for prudent trust management. In addition to requiring trustees to account to beneficiaries, the law offers mechanisms for trustees to have their decisions and actions approved, thereby defining the scope of their liability. For example, a trustee may seek to have the trust beneficiaries consent to a specific transaction or to all transactions and trustee decisions during a specified time period. Trustees who are subject to direct court jurisdiction may be required to submit accountings for formal judicial approval. Even absent such requirement, a trustee may seek protection and finality by asking a court for approval of specific matters or of all transactions during a particular period of time. Accountings for prior periods are also essential when there is a change of trustee, to ensure that the successor trustee begins his or her responsibilities with full knowledge and a clean slate.

5. **Form of Accountings**. While there is a trend towards uniformity in trust accountings, the proper form of a trust accounting varies depending upon applicable local law, local practice and the specific circumstances of the trust. Most accountings should be prepared on an annual basis and should show initial assets, income and principal transactions and assets on hand at the end of the year. Obviously, the accuracy and completeness of accountings, and the efficiency of their preparation, will depend upon the trustee maintaining accurate and orderly trust records. Indeed, if a trustee's actions are challenged in court the quality and accuracy of the accountings and records could have a material effect on the outcome of the case.

G. COMPLIANCE WITH TAX LAWS

A trust is normally a "taxpayer," with its own tax identification number and obligation to file income tax returns with the United States Treasury and probably with at least one state or other jurisdiction, and to pay taxes due including estimated taxes if required.

The trustee must also comply with transfer tax laws such as the estate tax and generation-skipping tax and the rules for filing of relevant returns and payment of those taxes.

Income Taxes. Trusts generally are tax-paying entities, but may trusts do not pay income taxes. It is important for the trustee to understand the nature of the income taxation of trusts, or to retain an advisor who will provide assistance in this regard. State laws for taxation of trust income vary widely from state to state, and a trust may be subject to income tax in more than one state. A significant factor is that the federal marginal tax rates on trust income reach the highest rates at $11,150 of trust income for the year 2008.

For Federal income tax purposes, there are three types of trusts (other than those for charitable purposes). In the case of *simple trusts*, which are those required to distribute income currently, the recipient beneficiaries pay the tax on whatever income is taxable, which may include the value of non-cash assets actually distributed as well as certain income which may not have been distributed.

In the case of *complex trusts*, which are those whose trustees have discretion over whether income is distributed to the beneficiaries, any income not distributed to the beneficiaries during the taxable year of the trust will be taxed to the trust or it may be taxed to the grantor, whether distributed or not (if the trust is a "Grantor" trust). That third type includes revocable trusts, but it may also include certain irrevocable trusts due to special tax rules that may cause a person having certain powers over the trust to be treated as "grantor" of the trust for income tax purposes.

Generally, the trust pays tax on net capital gains realized by the trust, even if principal is distributed to beneficiaries in the same year, although there are some exceptions to that rule.

Other Income Tax Considerations. Assets included in the gross estate of a deceased trust grantor receive an adjustment in tax basis for Federal income tax purposes at the grantor's death, subject to special rules. That adjusted basis is a factor that a trustee needs to consider in deciding whether to distribute trust assets during the grantor's lifetime, rather than continuing to hold them until the grantor dies. A similar analysis would be required when a trustee considers whether to retain a power which would cause the inclusion of the trust assets in the trustee's estate, or to renounce that power in order to keep the trust assets out of his or her estate.

Charitable Trusts. Special provisions of the tax laws apply to trusts established entirely or partially for charitable purposes. Even if income is exempt from tax, the trustee will probably be required to file tax returns. Special assistance of qualified tax counsel should be obtained.

H. COMPLIANCE WITH OTHER GOVERNMENT REGULATIONS

A Trustee should acquire at least a general idea of the impact of the securities laws as they apply to persons who invest other people's money. The applicable body of Federal law is the Investment Advisers Act of 1940, and there are complementary state statutes in effect in each of the fifty states. A person undertaking an occasional trusteeship, and not on a professional basis, may have no involvement with those laws, but every trustee is well advised to seek qualified legal counsel for guidance as to the need to register or otherwise comply with those laws.

Courts of probate jurisdiction exercise broad authority over many categories of trusts, particularly those provided under decedent's Wills. All practicing lawyers who are familiar with probate law practice will know the requirements for such procedures as the following: being appointed trustee, posting required bonds and, if required, sureties, obtaining judicial instructions when necessary, and submitting proper accountings to the court, the beneficiaries and, when there are charitable interests, to the state attorney general or other legally designated overseer of charities.

In all types and areas of compliance with laws and regulations, and throughout the course of administering a trust, the trustee should seek qualified legal advise as to peculiarities of local law and any aspect which is not thoroughly within the knowledge of the trustee.

I. A TRUSTEE'S CHOICE, USE AND COMPENSATION OF ADVISORS AND SERVICE PROVIDERS

Upon undertaking a trusteeship an individual trustee must provide for a variety of services to implement the administration of the trust. Those services will be required to fulfill some or all of the following functions:

1. arranging for safekeeping of trust property;
2. maintaining an accurate and efficient system for processing and accounting for the receipts, disbursements, investments and distributions from the trust;
3. accurately reporting the accounting and other relevant trust information to the beneficiaries on a periodic basis;
4. arranging to make distributions and disbursements from the trust on a timely basis;
5. engaging competent counsel to advise on legal and compliance issues, including compliance with the requirements of any court which has jurisdiction of the trust;
6. obtaining competent fiduciary income tax return preparation services;
7. engaging competent advice for the continuing investment of the trust property; and
8. providing adequate liability and fidelity insurance.

Many of the foregoing services are available through a single provider, such as a suitably equipped bank, trust company or law firm. In other instances the services will be "unbundled," meaning that different aspects will be furnished by separate individuals or organizations. Although the trustee may delegate some of those functions to providers, the trustee is ultimately responsible to the beneficiaries for the proper administration of the trust. In this regard the trustee may aptly be considered to be the "captain of the ship." Thus, the trustee must make sure that any service provider he or she engages for the trust is fully capable of handling the assigned task and has adequate information to do so on an ongoing basis.

While the trustee may delegate certain trust functions to an outside provider, he or she should recognize that some decisions or responsibilities are personal to the trustee and cannot be delegated to anyone. Most importantly, the trustee alone must determine how, when and to whom trust property will be distributed. The trust instrument will frequently describe those functions that the trustee is required to carry out "in his or her sole and absolute discretion," such as deciding whether to make a discretionary distribution of trust property or whether the trust should be terminated before the specified termination date.

For many years the laws of most states required a trustee to make all investments decisions and did not allow those decisions to be delegated to an investment advisor. However, "Prudent Investor Rule" statutes enacted recently in many states including New York do permit the trustee to delegate investment decisions to an independent advisor *provided he or she exercises reasonable care in selecting the advisor, establishes that the delegation is consistent with the terms of the trust, and monitors the investment performance on a regular basis.*

Presumably the trustee will pay outside organizations or individuals for the services they provide to the trust, such as custody, accounting, tax and investment advice. While it is appropriate, depending on the terms of the governing instrument, for trust funds to be used to pay for these services, the trustee should review the costs of administering the trust (including the trustee's own compensation) to make sure that the total is reasonable and does not exceed the amount allowable under the governing instrument of the law of the state where the trust has its *situs* or "legal home."

J. **A TRUSTEE'S COMPENSATION AND LIABILITY**

A trustee who performs the prescribed duties, and who does not exceed the proper limits upon the trustee's powers, is entitled to financial compensation for his or her services. Conversely, a trustee who fails to perform duties properly, or who exceeds limits on powers, may have legal liability to the trust and its beneficiaries.

Trustee compensation is governed by laws of the state in which the trust is administered and also by the terms of the governing instrument. In some states like New York a fee schedule is set out by statute or court rules. See NY Surrogate Court Procedure Act ("SCPA") § 2309. Alternatively a fee schedule may be described in the governing instrument. The trustee is also entitled to reimbursement for out-of-pocket costs that have been incurred. If there are more than two trustees, no more than two commissions shall be allowed unless the decedent has expressly provided otherwise in writing and the compensation must be apportioned according to the services rendered by the trustees unless they agree otherwise. See NY Surrogate Court Procedure Act ("SCPA") § 2313. Fees paid to attorneys, accountants, investment managers, and the like may be separate and in addition to the trustees' fee; however, to the extent that those fees are for services normally provided by a trustee, they may reduce the compensation to which the trustee is entitled.

If an individual trustee is a member of the beneficiary family, particularly if not a trained or professional fiduciary, it should be made clear in the governing instrument whether or not the trustee is to be entitled to compensation.

Trustee Liability. A trustee can become *personally liable* for a breach of duty as trustee when the breach results in a loss to the trust; however, the trustee is not a guarantor of the principal and income of the trust and usually will not be liable for losses that occur despite faithful performance of his or her duties. Grantors commonly provide in trust instruments that a trustee may have some measure of exemption from liability. Different states have different provisions regarding accounting and whether such an accounting starts the statute of limitations running so that after the relevant period of time the trustee would no longer be liable for an act which has occurred in the past. The trustee may also be liable for the actions of agents such as an investment manager, unless there is specific authority for delegating responsibility to the agent and relying on the agent's advice. For example some trust instruments and some state laws like New York provide that if an investment manager is selected with care, and the actions of the investment manager are reasonably monitored from time to time, the trustee is not personally liable for losses from investments chosen by the investment manager. In states like New York which have enacted the Prudent Investor Rule, a trustee, with advice of legal counsel, may wish to look into possible options for delegation of investment decisions to a qualified investment advisor, and, at least in theory, to be relieved of liability if he or she performs the required degree of monitoring of the work of the investment advisor.

Removal. In addition to a potential liability of a trustee, an additional remedy may exist for aggrieved beneficiaries. A court having jurisdiction over the trust generally will have power to remove a trustee in cases where there has been a breach of duty by the trustee or other misfeasance. Further, it is sometimes provided in trust instruments that beneficiaries have the power to remove a trustee, either with or without cause.

K. RESIGNATION

There is perhaps no more powerful measure of the seriousness of an appointment as trustee than the fact that once the appointment is accepted the trustee generally may not unilaterally resign or refuse to continue acting for the trust. There are two major exceptions. First, the provisions of the trust instrument may provide a method for resignation and even establish a procedure for appointment of a successor trustee. Second, the trustee may follow applicable legal procedures to secure a court approved resignation. Those exceptions, however, are not substitutes for the trustee's careful consideration of all relevant circumstances before accepting the trusteeship.

Resignation by the Terms of the Trust Instrument. The trust instrument may provide the trustee with a method of resigning as well as a procedure for the appointment of a successor trustee. If such language is clearly contained in the trust instrument, the trustee must follow those written provisions. That should include attention to (a) the trust instrument's procedure for the appointment of a successor trustee who is willing to accept such appointment, (b) the resigning trustee's obligation to furnish accountings to the beneficiaries, and (c) the delivery of the trust assets to the successor trustee.

Resignation by Judicial Procedures. If the trust was created under a Will, or if it is already subject to current supervision of a court, the rule is quite common that the trustee must petition the court having jurisdiction for permission to resign, regardless of the provisions contained in the Will. Likewise, if an inter vivos trust instrument does not provide a clear and specific procedure for resignation, the trustee would have to petition the court having appropriate equity jurisdiction over the trust for permission to resign. The court may accept the resignation of the petitioning trustee and appoint a successor trustee, but the court does not necessarily have to do so. The primary concerns of the court will be that the trust assets be preserved and that the trustee's resignation is in the best interests of the trust's beneficiaries . The court will insist upon (a) the availability of a suitable successor trustee who is willing to accept such appointment, (b) the resigning trustee's obligation to furnish accountings to the beneficiaries, and (c) the delivery of the trust assets to the successor trustee.

L. CHOOSING TRUSTEES

At least one trustee must be named when a trust is established. That may be a qualified individual or an institution having trust powers under applicable law. Successors also may be named, in case the initial or prior trustee resigns or otherwise ceases to serve. Sometimes a trust instrument will describe a procedure by which successor trustees are to be selected.

The duties and responsibilities of a trustee are varied. Some consider it difficult for one individual to carry out all of the duties and responsibilities of a trustee; however, an individual trustee may, in most cases, engage the services of advisors to assist the trustee. The other option is to name a corporate trustee, intending that the corporate trustee would undertake all of the duties and responsibilities of a trustee itself, without delegating them. (References to a "person" in the following text will include corporate as well as individual trustees.)

What are the primary considerations in deciding whom to select to be trustee?

1. **Responsibility and Reliability.** The trustee selected should be a person who can be relied upon to carry out his or her duties in a timely and responsible manner. If there is any question whether that will be difficult for that person to accomplish, then perhaps a co-trustee, with capabilities that complement those of the other trustee should be considered.

2. **Experience and Expertise**. A candidate for trusteeship should have had experience as trustee or at least analogous experience. Is there particular expertise that the candidate would bring to the task, given the type of assets likely to be administered and the problems to be faced? What are the options of others who have dealt with the candidate in relevant circumstances?

3. **Conflicts**. Does the candidate occupy a position that might create conflicts of interest, real or imagined? For instance, is the person a family member who has problems dealing with other family members who will be beneficiaries? Is the person a co-owner or business partner in a business or entity that will have to be administered by that person as trustee? Would selecting a different person be more desirable in those cases?

4. **Availability and Communication**. Geographic proximity to the beneficiaries is usually desirable, but the technology now available reduces the impact of this factor. Nevertheless, a key consideration in selecting a trustee is the likelihood that the trustee will be available to the beneficiaries of the trust and will be a good communicator. A lack of communication skills or a reluctance of the trustee to be available to the beneficiaries may cause problems over the years.

5. **Term of the Trust**. How long a trust is anticipated to last may impact the choice of trustee. A person who is aging rapidly, has health problems, or is too busy, would generally not be a good candidate for a long term trusteeship. Also, for longer duration trusts, a succession of trustees should be provided. A corporate trustee can usually be counted on to be available for the duration of a longer term trust.

6. **Fees**. It is generally understood that corporate trustees charge fees based on a percentage of the trust's income or principal or both. In smaller trusts that can be expensive (especially where minimum fees are used). Family members often serve without fees, or with relatively minor fees, but they usually need to hire and compensate investment advisors, accountants and/or attorneys to assist them in carrying out their duties. Generally, those fees can be negotiated, and may be payable out of trust assets if the trust instrument or local laws permit.

7. **Summary**. The various considerations above must be weighed in determining who would be best suited to act as trustee. There is not always a good or clear answer. Because the initial selection may not work out, it is advisable to build into the trust agreement a process for the trustee to resign or the adult beneficiaries (or some designated third party) to remove the trustee and, in either event, to appoint a successor trustee. Trusts are not static. The types of assets being administered, as well as other needs of the beneficiaries, are apt to change significantly over the years. In selecting a trustee one should anticipate the changing nature of the trust's assets and the changing composition of the group of beneficiaries as well.

In the event of resignation or removal or a trustee's death a successor trustee *must* be appointed. Often the trust instrument will name a successor and the successor can either accept the appointment or not. If the former trustee is still alive, the former trustee has the duty to transfer all assets and pertinent records to the successor. In the event of the death of an individual trustee the responsibility for those actions would fall upon the personal representative of his or her estate. If there is a successor trustee appointed by the trust instrument, generally a financial institution or title company will recognize the affidavit of death of the former trustee signed by the successor trustee together with a copy of the trust instrument as sufficient to pass title. Alternatively, if the Court has appointed a successor trustee, the certificate of appointment by the Court will be sufficient to enable the new trustee to obtain title to the assets. The successor trustee, like an initial trustee, has the duty to see that all the assets are collected.

As the foregoing discussion implies, it is often desirable to arrange for two or more trustees to serve concurrently, rather than to have one serving alone. Especially if the potential sole trustee is to be an individual, rather than a corporate trustee, there can be tremendous advantages in having co-trustees to share the required exercised of judgment, as well as to assure continuity if one of them becomes unable to perform. In fact, even with a corporate trustee it is often desirable to appoint an individual co-trustee to serve concurrently to provide a personal touch and oversight.

AFTERWORD

To summarize, a trusteeship requires many disciplines, such as: painstaking attention to detail, dogged emphasis on the safety of the trust's assets, a prudent and appropriate effort to maintain and enhance the investment value of the trust assets, awareness and management of continuing cycles of deadlines, and adequate maintenance of communications with beneficiaries.

This *Guide* comprises a consensus of suggestions and consideration, and that no written words, set down at one time, can fully described all of the contingencies which may occur in the future to test the trustee and, ultimately, the person or persons who appointed the trustee. Given those limitations, the over-riding quality of a trustee should be sound judgment, and the ability to exercise that judgment, and the ability to exercise that judgment fairly in the myriad of circumstances which may arise as long as the trust continues.

APPENDIX A
TYPES, PURPOSES AND PROVISIONS OF TRUSTS

Trusts almost always are established by the terms of a written instrument, which may be the Will previously executed during the lifetime of a person who has died, or it may be an *inter vivos* instrument executed by a living person and which is effective immediately.

Trusts are created for a variety of purposes, but there are a few typical trusts that are the ones used most often in estate planning. Understanding the type and purpose of the trust is key to understanding the duties of the trustee. In common usage the governing instrument may be loosely referred to as the "trust," but strictly speaking the "trust" is the legal entity created under the instrument governing it.

***Inter Vivos* Trusts (Including "Living" Trusts)**. *Inter vivos* trusts are trusts created during the lifetime of the grantor. *Inter vivo trusts* are either revocable or irrevocable by the grantor. *Inter vivos* trust instruments are most typically called "agreements" or "indentures," or sometimes "declarations" if the grantor is the trustee. *Inter vivos* trusts which are revocable are commonly referred to as "living trusts" and are often created to hold assets in the expectation that they should not be subject to the probate court process following the death of the grantor. Living trust commonly continue after the disability or death of the grantor and the trust instrument spells out the subsequent terms of the ongoing trust. One common type of irrevocable *inter vivos* trusts is insurance trusts that are designed to hold life insurance so that the insurance proceeds are not included in the taxable estate of the grantor. Other types of irrevocable trusts are designated to hold lifetime gifts, as, for example, where the beneficiaries are minor children or are otherwise incapacitated and unable responsibly to manage the donated assets.

Testamentary Trusts. Testamentary trusts are created under the will of someone who has died and thus come into being only at the death of that person.

Common Subtrusts. Either in a Will or in an *inter vivos* trust a married person might create subtrusts that would come into effect upon the death of whichever spouse dies first, and then continue for the lifetime of the surviving spouse. Examples would be a "marital deduction trust" or QTIP trust intended to qualify for the estate tax marital deduction and a "credit shelter trust" or similar entity designed to hold assets qualifying for the grantor's exemption from estate tax. Such trusts often also provide family subtrusts or separate shares for children or other ultimate beneficiaries.

Generation-Skipping or "Dynasty" Trusts. Trust that are intended to take advantage of the exemptions from the federal generation-skipping transfer tax, benefiting distant or multiple generations of a person's descendants, are sometimes called generation-skipping or "dynasty" trusts.

Charitable Split-Interest Trusts. Another common type of trust would benefit one or more individuals and one or more charities, often called a "charitable split-interest trust." The federal tax law imposes strict restrictions on the types of charitable split-interest trusts that qualify for the charitable income tax and estate tax deductions. A common type of charitable split-interest trust is a charitable remainder unitrust that benefits a family member or members for life or a period of years, after which the trust estate is to pass to one or more charities.

Changing the Terms of a Trust Instrument. Generally a trust instrument provides explicitly whether it is "revocable" or "irrevocable." If a trust instrument is revocable, it may be changed by the grantor or someone else, by following the procedures established under the trust instrument. If a trust instrument is irrevocable, it cannot be modified unless a court having jurisdiction over the trust orders a modification, following what is essentially a trial involving all persons interested in the trust. Under certain circumstances the Court will allow a modification of the terms of the trust and/or its termination if all the beneficiaries, including representatives such as guardians *ad litem* for unborn beneficiaries, consent to the change or termination. For example, a Will may have created a trust that was of sufficient size to be practicable when the will was written, but with the passage of time it may become so small as to be uneconomical to administer and the Court might order the distribution of the trust assets to such of the beneficiaries as the Court determines would most closely honor the intent of the decedent.

APPENDIX B
A LIST OF TRUSTEES' TYPICAL RECORDS

Legal Records

1. Governing instrument(s) (including disclaimers or documents exercising a power of appointment)

2. Written evidence of the resignations and appointments of trustees, preferably the signed resignations and appointments themselves.

3. Court filings with respect to the trust (e.g., accounts, petitions for adjudication, schedules of distribution, petitions for appointment or resignation of trustee, with all attendant papers)

4. Court judgments and decrees with respect to the trust and its trustees

5. Out-of-court agreements regarding administration/distribution/termination of the trust

6. Agreements with respect to trustee compensation (including fee schedules, formal waivers, etc.)

7. Tax receipts with respect to the trust fund

8. Legal opinions furnished by counsel to the trustee

9. Record of discretionary actions taken, and the basis for same.

10. Record of investment decisions made, and the basis for same

11. Record of adjustments between principal and income (if permitted by local law) and basis for same.

12. Record for selection/change of advisors (legal, investment, or tax) and basis for same.

Financial Records

1. Tax returns (income, gift, estate, real estate, employment, etc.)

2. Asset and transaction statements

3. Deed, certificate, etc. of any non-financial asset owned by the trust

4. Tax basis of trust assets

5. Appraisals of trust assets

6. Accountings

Operational Records

1. All correspondence sent or received by the trustee in his or her role as trustee

2. Current family tree for beneficiaries

3. For each beneficiary: name, tax identification number, address, telephone numbers and email addresses; date of birth, adoption, marriage, divorce, and death; and circumstances, if any, of incapacity

4. For each trustee: name, address, telephone numbers and email addresses