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Picking a Trustee, Family or Banker?

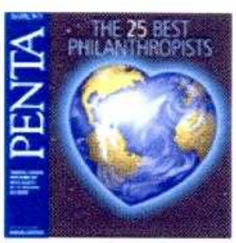
By KAREN HUBE

Plus, the new caution in trust investing.

IS THE TRUSTEE YOU'VE NAMED TO MANAGE your trust assets really up to the task? That question is suddenly getting a lot more attention.

Traditionally, most people have appointed family members, rather than bankers, to watch over the assets in their estates. But the turmoil in the the economy over the past 14 months has highlighted just how onerous the job of trustee can be. Not only are trustees charged with making sure assets are invested wisely; they also must be able to evaluate requests for distributions of cash to beneficiaries. In hard times like these, those requests can be both frequent and extremely touchy.

"We're seeing a lot of people question the savvy of family members handling things," says Alan Augulis, an estate-planning lawyer in Warren Township, N.J. "They are looking more toward established financial institutions when it comes to assigning a trustee."



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But that isn't the only answer. You can also appoint co-trustees, representing both the family and a financial institution established in trust services. And increasingly, experts are recommending three trustees -- two family member and one hired hand.

A trust is as simple or complicated as you make it: It's an empty vessel until you assign it assets and instructions for how and when you want the assets distributed.

Generally, if you create a trust to last generations, or if your assets exceed the federal estate-tax exemption of $3.5 million, or if you have a special-needs child requiring close support for years to come, you should have a professional trustee in the mix. A good pro can bring continuity and a high level of investment, accounting and planning expertise, says Andrew Garson, an estate-planning lawyer with Garson & Slepian in Fairfield, Conn. But even in these cases, a family-member trustee or two can be named as well.

A SOLE PROFESSIONAL TRUSTEE makes sense if there is simply no trusted family member qualified for the job. To serve as a co-trustee, Augulis says, the most important characteristics of a family member are common sense and trustworthiness. For a family member to be sole trustee, there should be some financial experience and strong administrative skills.

Most folks assign family members as sole trustees, no matter what their skill sets. For one thing, they want to avoid the expense of a professional; fees typically run up to 1% of assets annually.

James Bennett

For John Welniak, 62, of Murrieta, Calif., keeping things in the family was an issue of trust. "I don't think it would be worth having an expert direct our trust after we're gone if they work for someone like Bernie Madoff," says Welniak, who has named one of his three daughters to be trustee.

Yet, as many are realizing these days, serving as a trustee is no easy task. A trustee has legal responsibility to oversee the trust according to the grantor's specifications and the beneficiaries' best interests. This typically means overseeing investments, tax issues such as filing annual returns, and administrative matters such as filing regular statements to beneficiaries.

"Being a trustee is complicated and fraught with risks," says Don Weigandt, a wealth advisor for JPMorgan Private Bank in Los Angeles.

You may be investing for several beneficiaries with different needs and varying investment time horizons. Often a trust will have one income beneficiary -- the surviving spouse -- and "remainder" beneficiaries, who receive what's left when the surviving spouse dies. "If you put most of the assets in bonds, you would be favoring the income beneficiary," Weigandt says. "You have to be very careful."

Typically, a trustee will hire an investment manager, accountant and lawyer, but the trustee has the ultimate fiduciary responsibility for the trust, says Pat A. Iezzi Jr., an estate-planning lawyer and CPA at Iezzi Law in Greensburg, Pa.

The trustee also has the job of fielding special requests from beneficiaries. "If Johnny or Suzy says, 'I really need money for my new Corvette or beach house,' it can be hard to say no, even if saying no is what the grantor would have wanted," Weigandt says.

Things can get especially awkward if one of multiple siblings is named trustee. When Hank Linhart's mother died three years ago and his three s iblings found out that he had been appointed sole trustee to her trust, emotions ran high.

"My sister and brother were both in accounting and business, so I knew they were better qualified than I was," says Linhart, an after-school enrichment coordinator in the New York City public schools. He felt guilty, and there were signs that the two siblings felt resentful and hurt, he says. "It was really stressful."

Teaming up with a professional trustee might have helped Linhart, but that kind of arrangement isn't without challenges. Gary Hager, a financial advisor and founder and president of Integrated Wealth Management in Edison, N.J., points out that two co-trustees can end up in a deadlock that stirs up bad feelings among beneficiaries.

To avoid this, he says, be sure the language in the trust describes the roles of each co-trustee and how to handle a deadlock. Or consider appointing two family members and one corporation as co-trustees, "so you always have one person who can be the tiebreaker."

CO-TRUSTEES, WHETHER TWO or three, can also help prevent fraud. "You can imagine how it can happen," Weigandt says. "A trustee gets laid off, income is gone, and unless beneficiaries are paying very close attention, it's very easy for the trustee to tap into a trust. These are the things people are thinking about these days."

Sadly, it's no longer enough to simply trust the trustee.

Dear Prudence

THE FOLKS WATCHING OVER TRUSTS, never the most venturesome investors, have become even more cautious over the past year.

Trustees, who are obligated under the Uniform Prudent Investor Act to invest in accordance with conservative terms, and to best suit beneficiaries, have responded to last year's market meltdown by pulling back from stocks, loading up on bonds and adopting new measures to ensure enough liquidity to meet distributions and other needs.

"The definition of what prudent investing means hasn't officially changed, but what has changed is people's requirements for how risk is managed," says Gail Cohen, the fiduciary trust counsel at Fiduciary Trust International in New York. "People's idea of what their risk tolerance is has changed, now that they have a better idea of what we mean when we talk about volatility."

According to a survey by the Family Office Exchange in Chicago -- an advisor to 330 family offices, which invest 97% of their investable assets in trusts -- stock exposure slipped from 28% in October 2008 to 21% by August of this year.

Fixed-income allocations initially shrank from 12% to 7% between October 2008 and January of this year, but since then have surged to 17% of the average portfolio, according to the survey.

John Buoymaster, president and director of portfolio management at Hall Capital, a San Francisco firm that manages trusts for clients with investable assets of at least $100 million, says that his firm has not only increased bond exposure in many trust portfolios, but is also clearly delineating what purposes bond investments will serve.

Bond investments can provide liquidity for distributions, as well as ballast against stock-market volatility. "We had bond dollars covering both purposes, but we are now more explicit about separating out the purposes for bonds as our clients have gotten more defensive," he says. "You don't want to be drawing down your ballast."

MANY TRUSTS ARE ALSO KEEPING MORE liquidity on hand to be in a better position to meet capital calls, which occur when private-equity, real-estate and other funds that have been pledged investments approach investors to collect.

"If you're a trustee and you're planning for what capital calls you might have, in the past you may have said you only need half of what the commitment is, because it won't be called all at once," says Kemp C. Stickney, chief fiduciary officer at Wilmington Trust in Wilmington, Del. "But there are no guarantees of that -- if you get the capital call, you have to pay it. Certainly we're taking a hard look at what liquidity is enough."

While families generally aren't fleeing hedge funds in trust portfolios, in many cases they are trying to reduce the risk by using separately managed accounts to get into them, according to John Benevides, president of the Family Office Exchange. A significant concern about investing in a hedge fund is typically a lack of transparency about how much risk the fund is taking. One important service the provider of the managed account can offer is to alert investors if a hedge fund is veering from its stated strategy, Benevides says.

Of course, being prudent doesn't always mean getting more conservative. The trustee also has the responsibility to grow investments, typically at least at the rate of inflation. Some demands to get conservative go too far, Stickney says: "With the market the way it has been, it's sometimes an uphill battle to convince a client that having some hedge-fund exposure makes sense."

-- *Karen Hube*

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