Choosing Wisely - Selecting a Trustee

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Many people use a revocable trust as part of their estate plan because of its probate avoidance and privacy benefits after death. In addition, many people, whether using a will or a revocable trust, want their beneficiary to receive assets in trust, rather than outright, for any number of reasons.

Once you have carefully decided on your estate plan, it is important to also carefully choose your trustee. The trustee will hold the investment and distribution power, and will be responsible for respecting and enforcing the terms of the trust as you have established them. A trust meant to protect assets is of little benefit if a poorly selected trustee squanders the assets. If your plan includes a trust - whether it is a revocable trust or an irrevocable trust for beneficiaries after your death - you should give careful thought to your trustee selection.

What Are Common Types of Trusts and Their Purposes?

One of the first considerations in selecting your trustee is the type of trust your trustee will administer. Because different trusts may require different trustee roles, selection of your trustee should, in part, be driven by the type and purpose of the trust.

Revokeable Trusts

A revocable or "living" trust is designed to hold your assets during your life. Most often, you will serve as the initial trustee of your revocable trust. However, if you become incapacitated or are unable to manage your financial affairs, your successor trustee will step in. The role of your successor trustee will be to manage the assets in your trust for your benefit and to make distributions to you or for your benefit to ensure that your needs are met. You want someone who is going to be aware of your needs and situation and will act in your best interests.

After your death, the role of your trustee will shift. Your revocable trust becomes "irrevocable" and its terms establish how your assets will be distributed, much like a will would. At this point, your trustee's role will be similar to the role of an executor under a will. Your trustee will be responsible for collecting, managing, and distributing your assets to your beneficiaries (or to trusts for their benefit, described below) in accordance with your trust agreement.

Irrevocable Trusts

Any trust for a beneficiary established under the terms of your revocable trust or by your will and funded after
your death is an irrevocable trust. Likewise, in certain circumstances, you might establish an irrevocable trust during your lifetime, which means that you relinquish the right to change or terminate the trust. With any irrevocable trust, you must understand that you will be relying heavily upon your trustee to carry out your intent and the terms you have established in your trust.

Below are some of the purposes, including tax and non-tax reasons, for including an irrevocable trust in your estate plan:

- Irrevocable trusts frequently are used for estate tax planning. For example, establishing a "credit shelter trust" for the benefit of your surviving spouse will preserve your estate tax credit and shelter assets in the trust (and any appreciation on the assets) from taxation in your spouse's subsequent estate. If your taxable estate is in the ballpark of $5,490,000 individually, or $10,980,000 as a married couple as of 2017, your planning likely includes an irrevocable trust.
- An irrevocable trust can be used to control the disposition of your assets in the future. For example, in a blended family scenario where each spouse has children from prior marriages, an irrevocable trust will allow you to not only provide for your spouse, but also to control the disposition of the assets remaining in the trust following your spouse's death, including, if you desire, a requirement that all or a disproportionate share of the assets be directed to your children rather than your spouse's separate children.
- If you have a beneficiary who is too young to manage assets or otherwise is not financially responsible, an irrevocable trust may be appropriate in order to preserve and manage the assets you are designating for that beneficiary. Your trustee can judge how to distribute trust assets in a way that will make them last.
- Oftentimes, an irrevocable trust is chosen because of its asset protection benefits. Assets received in certain trusts are immune from claims of a beneficiary's creditors. Many people consider creating an asset protection trust if their potential beneficiary has heightened exposure to lawsuits because the beneficiary is involved in business or a high-risk profession (such as a doctor), or if the beneficiary is or may be involved in a divorce or similar dispute.
- Finally, an irrevocable trust often is used for a beneficiary with special needs. A special needs trust can be set up in a way that will not affect your beneficiary's receipt of governmental benefits. Similarly, if your spouse may need to qualify for Medicaid in the future, assets received in certain trusts will facilitate this.

In any of these scenarios, your trustee will manage the assets of your irrevocable trust and make distributions for the benefit of your beneficiaries pursuant to the terms set out in your trust agreement.

**What is the General Role of a Trustee?**

The trustee you select will have special obligations to you as the creator of your trust, as well as the beneficiaries of your trust. The trustee's duties arise under the terms of your trust agreement as well as under North Carolina law. Some of the essential obligations include:

- **Administering a trust by its terms.** First and foremost, your trustee must administer your trust in good faith and in accordance with the terms and purposes you have established in your trust agreement.
- **Exercising skill and care.** Your trustee must administer your trust as a "prudent person" would. In taking any action, your trustee must consider your trust's purposes, terms, distribution requirements, and other circumstances of your trust and its beneficiaries.
- **Duties of loyalty, fairness, and impartiality.** Your trustee must act in the best interests of your beneficiary. This means that your trustee must avoid situations in which your trustee's personal interests conflict with those of your beneficiary. If your trust has more than one beneficiary, your
trustee's decisions must be made by weighing each beneficiary's interests.

- **Managing trust assets appropriately.** Your trustee must invest and manage trust assets as a "prudent investor" would. This means that your trustee must consider the investments in the context of your entire trust. For example, an appropriate investment may depend on your trust's need for liquidity to make distributions, the types of assets in your trust, your beneficiary's other resources, or general economic conditions. Your trustee can delegate investment decisions to a financial advisor, but will still have an obligation to carefully select the advisor and monitor performance.

- **Keeping records and communicating.** Your trustee must keep records in connection with the administration of your trust, and provide information to your beneficiary as required in your trust agreement.

**What Factors Should You Consider in Selecting Your Trustee?**

*Trust purpose.* As noted earlier, you must consider the purpose of your trust. If the primary purpose is to provide asset protection for your beneficiary, it may be okay for your beneficiary to serve as trustee. However, if the goal of the trust is to preserve assets for a spendthrift beneficiary or for future generations, it could defeat the purpose of the trust for your beneficiary, or someone the beneficiary can influence, to serve as trustee.

*Family dynamics.* In addition, you should consider the relationship of your trustee and your beneficiary. Are they generally going to be able to work together? Will your trustee be comfortable standing up to your beneficiary if necessary? In tricky family circumstances, the best option for the trustee may be an unrelated third party, a bank, or a trust company.

*Judgment and experience.* Trust assets can waste away while under the care of an inexperienced trustee. A good trustee will exercise sound judgment in making investment and distribution decisions. Depending on the level and type of assets in your trust, the investment experience of the trustee can be important. A trustee experienced in handling such assets, or working with an investment advisor, can increase returns.

*Awareness of your beneficiary’s needs.* A trustee often has some degree of discretion in determining whether to make distributions to a beneficiary. Your trustee should be someone who will be aware of, and sensitive to, your beneficiary’s needs. You may want to consider a trustee who lives in the same community as your beneficiary, or is personally close to your beneficiary.

*Fairness.* The lack of a conflict of interest is important in selecting your trustee. For example, a trustee who is a potential future beneficiary of your trust may be reluctant to make distributions, even if the current beneficiary needs them because a distribution now will lessen the amount of trust assets that will be available to your trustee as a beneficiary later. A good trustee will be able to make decisions without being influenced by personal interests.

*Attention to Detail.* Managing assets and keeping track of distributions and other trust matters requires a certain level of accountability and attention to detail. Your trustee ideally should be organized and responsible.

*Tax factors.* If your trust is part of an estate tax reduction strategy, there may be important tax considerations in choosing your trustee that are beyond the scope of this article. Your attorney can guide you in this regard.

Finally, the selection of your trustee should not be a decision that is made once and never revisited again. You should "kick the tires" on your estate planning documents every few years to make sure that your trustee selection (and the rest of your estate plan) is still appropriate. If you find that amendments to your plans and
changes to your trustee are needed, you should act accordingly.

There are many reasons for using a trust in your estate plan. To achieve your goals in using a trust, it is important to choose your trustee wisely. A good trustee will exercise sound judgement, be fair, and follow the terms of your trust as you have created them, keeping your intentions in mind. If you cannot identify an individual who fits the bill, a corporate trustee is always an option.

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