WEALTH MANAGEMENT

Orange Bank & Trust Company
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Middletown, New York
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December 2016

# What does a trustee do?

***Many wealth management plans are built around family trusts. Selecting the right trustee is a key element for success.***

So you've decided on a trust plan. Perhaps it's a trust for a surviving spouse, one that will qualify for the marital deduction. Or a bypass trust, to bring a measure of control to the impact that death taxes could have on the family fortune. Maybe you've decided that a charitable trust is an excellent approach to meeting private and philanthropic financial goals. Or you might simply be looking to arrange for yourself the many benefits of a living trust.

That decision leads to another, equally important one. Who should be your trustee?

### *Duty calls*

The American College of Trust and Estate Counsel (ACTEC), a professional organization of lawyers dedicated to improving probate and trust practices, created "What It Means to Be a Trustee: A Guide for Clients." The purpose of the Guide is to familiarize nonlawyers with the true dimensions of trusteeship, and to assist them in selecting the right fiduciary for their families. One key task: translating the "fiduciary duty" that every trustee owes to trust beneficiaries into specific tasks. The group identified 13 distinct duties.

• ***Duty to administer a trust by its terms.*** Every trust agreement should make plain the purposes of the trust, as

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they provide the critical benchmark for evaluating the trustee's actions.

• ***Duty of skill and care.*** A high standard of performance is required, even if an amateur is named who has no prior experience as a trustee.

• ***Duty to give notices.*** Notices may concern legal rights of the trust beneficiaries, such as a power to make withdrawals, or they may cover such ministerial matters as designating a successor trustee or an agent to assist in trust administration.

• ***Duty to furnish information and to communicate.*** The trustee must respond to requests from beneficiaries concerning the trust and its administration.

• ***Duty to account.*** A written accounting of the assets, liabilities, receipts and disbursements of the trust must be provided to the beneficiaries regularly.

• ***Duty not to delegate.*** Although a trustee may employ professionals to assist in trust administration, the trustee may not accept blindly the advice of such persons. The trustee retains supervisory responsibility. Matters concerning the exercise of judgment and discretion generally cannot be delegated.

• ***Duty of loyalty.*** Trusts must be administered solely for the benefit of the trust beneficiaries.

• ***Duty to avoid conflict of interest.*** This is closely related to the duty of loyalty, and may come up when a beneficiary is named as cotrustee. Generally, the trustee should not engage in transactions with the trust unless such activities are authorized by the trust.

• ***Duty to segregate trust property.*** Trust assets must not be commingled with personal funds or other nontrust assets.

• ***Duty of impartiality.*** The trustee must not favor one beneficiary over another, unless the trust document directs that providing for a particular beneficiary is a principal purpose of the trust.

• ***Duty to invest.*** Trust assets must not be left idle. In addition to making the trust investments, the trustee has a duty to diversify the investments and develop an asset allocation plan. This is a job for professional investors or corporate fiduciaries.

• ***Duty to enforce and defend claims.*** Reasonable steps must be taken to protect the trust from adverse claims and enforce the rights of the trust and its beneficiaries.

• ***Duty of confidentiality.*** Normally, the terms of a trust, the identity of its beneficiaries and their respective interests, and the nature of the trust assets cannot be disclosed to anyone except the beneficiaries and those who need such information in order to be able to administer the trust.

### Your trustee needs:

☐ integrity;
☐ investment experience;
☐ administrative know-how;
☐ tax and accounting capabilities; and
☐ people skills.

Those attributes describe us well.

## *Whom will you trust?*

Given this list of responsibilities, one quickly can see the value of corporate fiduciaries, organizations such as ours, dedicated to trust administration as a business. We are staffed for this. We have trained for it. We do it every day.

To learn more about how seriously we take our trusteeship responsibilities, we invite you to arrange a meeting with one of our officers at your earliest convenience. Talk over your family financial objectives. See how we can help. ☐

## If you've decided against a corporate fiduciary

If you've decided to name an individual as your executor or trustee, reflect upon these questions:

- Will the person also be your beneficiary?
- Do you owe this person money?
- Does this person owe you money?
- Does the person have an unusual need for money?
- Can your beneficiaries trust the person?
- Will the person work well with others?
- Will the person have enough free time to handle the job?

As you can see, there is a potential for conflict of interest and other difficulties when one turns to a friend, even one with excellent credentials.

# Tax reform and the Trump administration

In 1980 one major plank of the Republican platform was tax reform along the lines of the Kemp-Roth tax cut proposals. By August of President Reagan's first year in office, the Economic Recovery Tax Act of 1981 (ERTA) was law, dropping the top marginal tax rate from 70% to 50% along with a host of other tax-based measures for economic stimulus.

Tax reform was perhaps less central an issue in the just-concluded Presidential election, but candidate Trump advocated many fundamental changes. The House Republicans also have developed a blueprint for tax reform in recent years, so many concepts already have been fleshed out. The table below summarizes some of the key ideas.

These changes would be the most consequential since the 1986 Tax Reform Act, which included just two tax rates and no preference for capital gains over labor or interest income. The fact that Republicans control both houses of Congress could aid in making new tax legislation a reality, but historically major tax changes have been bipartisan affairs.

The biggest stumbling block for comprehensive tax reform in recent years has been in the scoring, the predictions of how much revenue will be raised and how the burdens will be distributed among income groups. Generally, the goal has been to simplify, while keeping the changes revenue neutral overall. The Trump plan likely would be scored as losing revenue, raising the issue of how to "pay for" the changes with other tax increases or spending cuts. The counter-argument is that revenue shortfalls may be made up by higher economic growth, at least to some extent.

| Tax | Current law | Proposed by Trump or the House Republicans |
|---|---|---|
| Individual income tax rates | 10%, 15%, 25%, 28%, 33%, 35% and 39.8% | 12%, 25% and 33% |
| Standard deduction | $6,300 single, $12,600 married filing joint | $15,000 - $18,000 single, $24,000 - $30,000 married filing joint |
| Capital gains tax rates | 0%, 15% and 20% | Same or reduced to 6%, 12.5% and 16.5% |
| Net investment income tax | 3.8% | Repealed |
| Alternative minimum tax | Applies to income over $53,000 single, $83,800 married filing joint | Repealed |
| Corporate tax rate | 35% | 15% or 20% |
| Federal estate tax | 40% of amounts over $5.49 million in 2017 | Repealed |
| Generation-skipping transfer tax | 40% of amounts over $5.49 million in 2017 | Repealed |
| Gift tax | 40% of amounts over $5.49 million in 2017 | Unclear, probably repealed |
| Capital gains at death | None, tax-free basis step-up | Gains in excess of $10 million may be taxed |

Source: M.A. Co.

### *Estate tax repeal?*

The revenue from the federal estate tax is a tiny portion of total federal tax receipts. It is a complex tax to administer and comply with, and it has long been hated by small business owners and farmers. For this reason most Republicans and many Democrats have favored repealing the tax completely.

The general public also favors ending the estate tax. Some observers find this attitude surprising, given how few estates are likely to owe the tax because of the large amounts exempt. In part, public opinion may have been swayed by the Republicans' rebranding the estate tax as a "death tax." However, there is also the phenomenon that people may hope to be beneficiaries one day, and they hope that their inheritance will be undiminished by taxes. If tax reform is enacted in 2017, there is a very good chance that it will include repeal of the federal estate, gift and generation-skipping transfer taxes.

But there still may be a "death tax." When the estate tax is eliminated the tax-free basis step-up at death will likely be gone as well. It may be replaced by "carryover basis," as was the case in 2010, the year without an estate tax. Or a tax may be imposed upon unrealized capital gains at death. That is how the Canadians do it already, and that is also a feature of the Trump proposal. There would likely be an exclusion for smaller estates.

Whether the estate tax is repealed or not, estate planning and trust planning will remain essential for affluent families in their wealth management. ☐

## Giving by millionaires

A study of the charitable giving habits of persons with net worth greater than $1 million and annual income of $200,000 or more was conducted by U.S. Trust and the Indiana University Lilly Family School of Philanthropy. Some 91.0% of this group reported making charitable gifts in 2015, compared to 58.8% of households overall. On average, they gave to eight different nonprofit organizations. Religious organizations were the greatest beneficiaries of these gifts, receiving 36.1% of the total, followed by basic needs groups at 27.9% and higher education at 8.4%.

The lion's share (88.1%) of donors made their charitable gifts directly from current income or assets, as opposed to structuring their gifts over a period of time, as with a trust. Donor-advised funds were used by 3.0%, a fast-growing category that nearly has overtaken charitable trusts at 3.3%. Some 2.5% made gifts from their family's private foundation. Structured charitable giving increases with wealth levels, as 44.5% of those whose wealth exceeded $5 million used some form of planned-giving vehicle.

Charitable giving will remain stable for the next three years for 55.1% of the donors, according to the report, and just 3.4% expect their contribution levels to decrease. Some 28.2% are planning to increase their donations in the coming years.

The competition for charitable gifts is intense, sometimes too intense. Some 17.1% of donors reported that they ended support for one or more charitable groups in 2015. Donors don't like to be nagged—getting too many requests or requests too close together in time was the most-cited reason for dropping donations to a charity. Here is the breakdown:

| | |
|---|---|
| 40.7% | Too many solicitations |
| 40.2% | Household circumstances changed |
| 18.0% | Charitable organization was ineffective |
| 14.0% | Donation requested was inappropriate |
| 12.8% | Donor changed philanthropic focus |
| 12.1% | Changed leadership or mission at charity |
| 9.6% | Charity failed to respect personal information |
| 3.9% | Charity met its goal, completed its mission |
| 15.0% | Other |

Tax considerations play a role in determining the size of a charitable gift, but perhaps not as great as the conventional wisdom might suggest. 62.4% of donors reported that they would make the same amount of charitable gifts even if the income tax charitable deduction were eliminated. The estate tax is apparently even less consequential, as just 4.6% of donors would reduce their charitable legacies if the federal estate tax were eliminated, while 23.2% would increase their charitable gifts at death, presumably redirecting to charity funds earmarked for death tax payments. ☐