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ORANGE Bank & Trust COMPANY

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WEALTH MANAGEMENT

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Who will be *your* trustee?

More and more affluent families are turning to trust-based solutions for family wealth and inheritance management. However, a trust plan is only as good as its trustee. Have you been asked to serve as trustee, perhaps for a parent's trust? Do you plan to ask your child to be your trustee? Although such a course of action may be a natural impulse, it may not be the best approach.

A family member has the advantage of personal understanding of the trust beneficiaries, and that is no small thing. Unfortunately, family members usually lack experience and ability in several other crucial areas.

The case for using a corporate fiduciary

Attorney Stuart Bear gave a fascinating presentation at the *2019 Heckerling Institute on Estate Planning,* titled "Why Can't My Brother-in-law Bob Be the Executor of My Estate?" He reviewed for the estate planners some of the important, practical considerations for choosing the best fiduciary to supervise the implementation of an estate plan, beginning with this job description:

1. Correspond with disgruntled beneficiaries;
2. Manage family drama;
3. Provide accounting to disgruntled beneficiaries;
4. Invest assets (don't lose money or you will hear from disgruntled beneficiaries); and
5. Receive phone calls from disgruntled beneficiaries inquiring when they will receive their inheritance (but remember, it's not about the money).

Some additional highlights from his talk are below.

Resist the first impulse

Very often someone's first thought in selecting an executor or trustee is that either a spouse or adult child can handle the job. It's vital to probe the family dynamics before moving ahead with such a decision. Sample questions might include:

- Do your children communicate regularly?
- How would one child react to his or her sibling receiving compensation for managing and distributing assets?
- Is any child likely to demand an inheritance immediately?

Most people need to be brought up to speed on what fiduciary duties are, how much time and expertise they may require, and the value of having an impartial third party involved in decisions that may be not always be popular.

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Individual fiduciaries

The benefit of naming an individual to serve as trustee chiefly is familiarity with the family values, family members, and family dynamics. There is a perception that an individual will be less costly, or may even waive fees for serving as trustee. Unfortunately, most individuals will need to hire experienced professionals to help in the discharge of their fiduciary duties, so the total cost of administration may actually be higher with an individual in charge.

Corporate fiduciaries

Corporate fiduciaries (such as us) bring experience, expertise, professionalism, and objectivity to the jobs of trusteeship and estate settlement. Continuity of service is another advantage. Although there may be employee turnover, and the banking industry has experienced a series of acquisitions and mergers, a trust division doesn't take vacations, get sick, or move out of state. Corporate fiduciaries are regulated and bonded.

Attorney Bear recommended interviewing a handful of candidates before deciding upon a corporate fiduciary. Sample questions include:

- What services will be performed?
- What services will *not* be performed?
- Are distribution requests handled by an individual, or by a committee?
- How long does it usually take to decide on a request for a discretionary distribution?
- At what asset level would the trustee terminate the trust and distribute the assets outright?
- Will specific language need to be included in the trust document?

For those who can't make up their minds, it may be possible to have multiple fiduciaries, a sort of "best of both worlds." However, someone needs to be in charge, and that should be made plain in the estate plan. Don't overlook the importance of planning for the selection of a successor trustee, perhaps through the appointment of a trust protector.

Family meeting

Attorney Bear offers to facilitate a family meeting for his estate planning clients, to be held in his office. To get everyone on the same page, he said, everyone needs to be in the same room. The meeting should include the nominated fiduciaries and the client's children. There is sometimes a question about including the spouses of the children, but Bear prefers to have them attend as well. It provides for better control of the message, and is more likely to reduce future conflicts.

A family meeting will be especially important for a second marriage or blended family situation, if specific property will go to specific beneficiaries, if assets will be distributed unequally, and if there will be a hierarchy in the nomination of fiduciaries. The goal is to avoid surprises and reduce future conflict after the death of a family member.

Bear opens the family meeting with a discussion of wills, trusts, and the respective roles and responsibilities of the personal representative, trustee, attorney-in-fact, and health care agent. He summarizes the planned distribution of assets, and then turns the meeting over to the client. The client then may explain the thinking behind the distribution plan and the choice of fiduciary or fiduciaries.

Bear concluded his presentation, saying: "Educating clients on fiduciary selection and fiduciaries on their duties can go a long way to ensure the success of any given estate plan."

The choice is yours

We invite you to learn more about our capabilities as trustee for your family. You may designate us to serve as sole trustee, or as cotrustee along with family members. Call on us to discuss the possibilities. ☐

Trustee checkpoints

To make an informed decision about your choice of trustee, think about questions such as these:

✔ Does the prospective trustee have the time and experience necessary to handle the job?

✔ Has the organization or individual performed capably in both bull and bear markets?

✔ Could conflicts of interest arise between your trustee and your family?

✔ Will each and every beneficiary be treated fairly and impartially?

✔ What fees will the trustee charge? Do the fees include investment management costs, or will they be an additional expense?

✔ Will your trustee provide recordkeeping at no additional cost?

✔ If conflicts develop between the beneficiaries, how will they be resolved? Will all the beneficiaries respect the decisions of the trustee?

The importance of dividends

When people talk about making money in stocks, they are usually referring to capital appreciation. After all, when we hear that the Dow Jones Industrial Average or the S&P 500 stock index has set a new record, it is the prices of the shares that is being referred to. But over the years, dividends have contributed importantly to the total return of stocks. A study by Standard & Poor's reported that since 1926, some 34% of the total return of the S&P 500 has come from dividends. In the 1940s and again in the 1970s, dividends were responsible for 50% or more of the total return!

Here's another way to look at that phenomenon. If you had invested $1,000 in the S&P 500 as 1926 began and held it for the next 95 years, your investment would have grown to $373,518. That assumes you spent your dividends as you received them. If instead you had reinvested those same dividends in the S&P 500, you would have accumulated $14,086,369! That shows the compounding power of reinvesting dividends. (Data from Kroll 2022 SBBI® Yearbook. Example for illustrative purposes only; you cannot invest in an index.)

The importance of dividends in the total return of large company stocks fell to 14% in the 1990s, when investors were hunting for lightly taxed capital gains instead of dividends. The trend began to reverse when qualified dividends were given the same favorable tax treatment as long-term capital gains. The graph below shows the recent history of stock returns, with and without dividend reinvestment.

New environment

However, the stock market as a whole is off to its worst start in more than half a century this year, losing some 16% in the first four months. Even so, stocks remain more expensive than normal. The average price-to-earnings ratio of the S&P 500 over the last 20 years has been 15.7, according to *The Wall Street Journal*. The multiple reached a high of 24.1 in September 2020. Now it is back down to 16.8.

The volatility in stock prices comes from the sharpest bounce of inflation in more than a generation, and uncertainty about how the Federal Reserve Board will respond to it. The cost of addressing the severe inflation of the 1970s was a sharp recession, which the Fed will be trying to avoid. The war in Ukraine adds still more uncertainty, with the prospect of severe disruptions in international trade. Rising interest rates will depress the value of existing bonds, which suggests that investors will have trouble finding a safe haven for their assets.

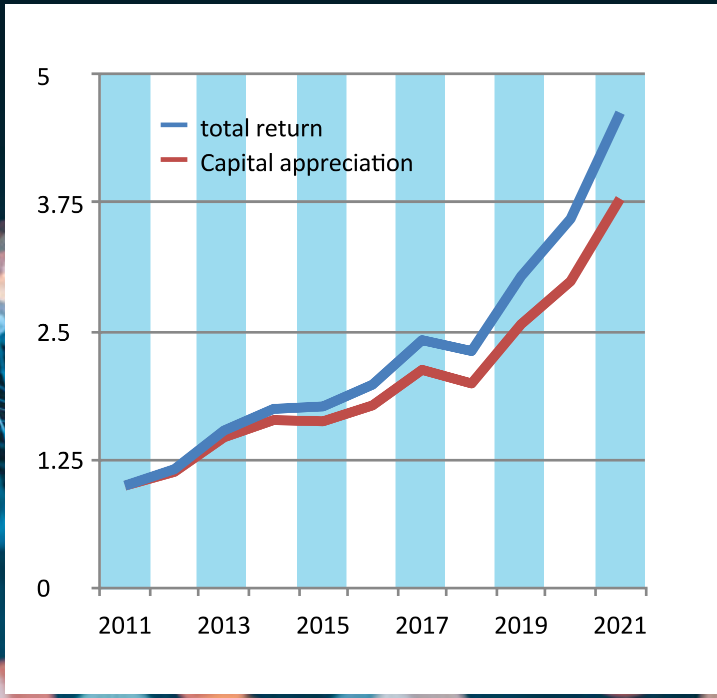
As a general rule, equity investments have been able to keep up with inflation, and bond portfolios have not, but the added return comes with added risks.

Are you confident with the role that dividends are playing in your portfolio planning? Would you benefit from getting a second opinion about your investment strategies? Please give us a call; we will be pleased to be of service in this regard. ☐

Dividend power

Over the past ten years, stock prices have trended upward, as shown by the red line in the graph below. The data is for large company stocks, and comes from the *Kroll 2022 SBBI® Yearbook*. The total return from stocks includes dividends as well, and those dividends are reinvested in stocks for compounding growth. The blue line shows the total return of large company stocks since 2011.

Source: Kroll 2022 SBBI® Yearbook



IRS report card

Last year the IRS was swamped by some 185 million attempted calls by taxpayers for tax information. This year there were only 39.5 million such calls to customer service lines, of which 2.7 million got through. These dispiriting figures are from a preliminary report of the Treasury Inspector General for Tax Administration (TIGTA).

On a more positive note, the Service identified 76,814 fraudulent tax returns in 2022, compared with just 2,325 in 2021. Some $808 million in false tax refund claims were blocked.

Leaker at large

In June 2021, internet publisher ProPublica released "The Secret IRS Files" based upon 15 years of tax returns of the top 0.001% of taxpayers. After reviewing data from an anonymous leaker, the report purported to show that wealthy Americans are undertaxed.

There was an immediate uproar over the violation of taxpayer confidential information, and a full investigation was promised. After nearly a year, we are no closer to understanding how the IRS data was compromised or stolen. Hackers might have been responsible, or perhaps an unscrupulous IRS employee did the deed. Treasury Secretary Janet Yellen, testifying before the Senate Committee on Banking, Housing and Urban Affairs in May, said the leak was "very damaging" and the department is doing "everything in our power to make sure there is not inappropriate access to such data."

Failure to resolve questions concerning the data leak has led to political opposition to proposals to expand information reporting to the IRS, and has been cited as a reason to oppose the IRS' hiring of more enforcement personnel.

Student loans and tax refunds

Between 1981 and 2002, Jeffrey Seto borrowed nearly $100,000 to fund his higher education. As of 2018, all the loans were in default, and interest and fees had ballooned his debt to more that $170,000. Mr. Seto began a repayment program, but soon fell behind.

In July 2019, Mr. Seto purchased a rooftop solar energy system for his home for $26,939. When he filed his 2019 income tax return, he claimed a credit for the solar installation of $7,994 and a total refund of $9,288. He was notified that the entire refund would be applied to his student loan debt.

Mr. Seto filed a lawsuit with the Federal Claims Court for recovery of his tax refund, acting as his own attorney. Unfortunately for him, that Court does not have jurisdiction to recalculate his loan obligations. What's more, the Department of Education had warned him that failure to keep up with his loan payments could result in wage garnishment or offsetting the student loan against tax refunds. □

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