

Fiduciary Obligations: What Trustees Must Know

MOST CLIENTS name themselves to serve as the initial Trustee of their living trust; couples typically serve together as co-Trustees of their trust.

Whether you begin as your own Trustee or assume the job as a Successor, this probably is your first experience as a *fiduciary*. This is a serious responsibility, so you need to do some self-education right away. I have written this brief memo to introduce you to the Trustee's role and to start you on your way.

As the legal owner of all trust property, the Trustee of a trust has a broad range of authority to be able to manage the trust and its assets, called the "*trust estate*". These powers are exercised within a structure of legal duties that the trustee owes to protect the trust assets and the interests of the trust beneficiaries.

The Trustee's job is a mix of responsibilities for which the Trustee is given considerable authority to carry out.

Trustee Powers. "*With great power comes great responsibility.*" We remember Uncle Ben saying this line in *Spiderman*, but the origin of the quote is most often attributed to Voltaire, not Stan Lee. I like it because the statement nicely encapsulates the Trustee's role.

Your trustee has the powers granted in your trust and as provided by California trust law. Most of the trustee powers described or alluded to in your trust are found in sections 16200-16249 of the California Probate Code.

Overall, the trustee has the authority necessary to perform his primary duty: to carry out the terms of the trust. Unless a power is limited or made conditional in the trust document, the trustee has the power to accept property into the trust, acquire property for the trust, maintain and repair trust property, deposit trust funds, invest trust assets, borrow money and use trust assets as security (encumbrance), lease and sell trust property, execute contracts on behalf of the trust, insure trust property, pay the financial obligations of the trust and make

distributions to beneficiaries, hire professional and non-professional assistance, etc. This by no means lists all possible powers of the trustee.

Problems are rare, but when they arise the court system is there to help verify the trustee's power to act and to order that the trustee's instructions be followed by anyone holding property belonging to the trust. One reason that these problems are rare is that the law allows that the trustee all powers necessary to carry out the purpose of the trust. Another is that trustees of most living trusts do not get involved in complex transactions unless your financial life is complex in itself.

Trustee Duties. Trustees have the special duties of a fiduciary to you and to all beneficiaries of your trust. This is a legal term having several meanings, as follows:

The trustee's first duty is to administer the trust by its terms for your benefit and, after your death, for the benefit of your beneficiaries. Again, although problems in this area are very unusual, the courts will help your trustee resolve any uncertainties in this area.

In general, the Trustee must administer the trust with reasonable care, skill and caution under the circumstances that a prudent person acting in a like capacity would use would use to accomplish the same or similar goals of the trust instrument. Here is a review of the trustee's duties, which may be found in section 16000 et seq. of the Probate Code:

The trustee must administer the trust solely in the interest of the beneficiaries. This duty of *loyalty* may be difficult when there are several layers of beneficiaries, such as present and future beneficiaries. What makes it difficult is the trustee's duty to deal *impartially* with the beneficiaries, taking into account their differing interests in the trust. It is not surprising, therefore, that the trustee may not borrow from the trust in most instances because that creates a conflict of interest between the interests of the

trustee personally and the beneficiaries whom he serves.

The trustee must *keep the beneficiaries reasonably informed*. Generally, beneficiaries may request a copy of the trust and are entitled to information about the trust and its administration, which the trustee must furnish on request. Special notice to the beneficiaries is required when the trust becomes irrevocable, such as when the creator of the trust (the Settlor) dies.

As part of this obligation to inform, the trustee has a *duty to account* to you (and other beneficiaries, when appropriate) and to furnish information concerning the trust, the trust assets, and the trustee's administration of your trust. The trustee generally must account to the beneficiaries annually, when there is a change in trustees, and when the trust terminates. This duty can be modified somewhat by the terms of the trust or waiver by the beneficiaries

The trustee must *protect* the trust property; to keep it safe and separate from any other property not belonging to the trust. *No commingling*. Protection includes a duty to *enforce claims that are part of the trust property* and *defend the trust against losses*.

Along with the duty to *make trust property productive* (income and growth), he has the discretion to *invest* trust property for this purpose. The trustee's investments must follow the Uniform Prudent Investor Act (Sections 16045-16054), unless the trust specifies otherwise. For example, you may wish to limit the types of investments your trustee may make to match how you invest your assets independent of the trust.

The trustee is primarily responsible to you and your beneficiaries for the proper administration of your trust. The trustee *may not delegate* others any part of his job that the trustee can reasonably be required to personally perform. This includes delegation among co-trustees, unless the trust document allows that. This does not mean that the trustee must do all the work. In fact, your trust document allows your trustee to hire accounting and other professional assistants when that would be helpful. These are not services the trustee would be required to do personally unless he

was a licensed lawyer or accountant. However, if the trustee has *special skills* like these, he has a duty to use them.

A conflict of interest or "*self-dealing*" by the trustee can be such a transgression. This does not mean that your trustee can never deal with the trust assets to his or her own benefit. In many trusts, for example, you and your family members serve as trustees and you intend things to be handled for the benefit of your family.

However, if the trustee personally and in his or her capacity as trustee of your trust have an interest in the same asset (e.g., as joint owners or partners), there is a real potential *conflict of interest* and it may not be proper unless the trust allows it. The trustee must be careful not to prejudice the interests of any trust beneficiary when dealing with trust assets in a way that might violate this responsibility.

I strongly urge trustees to first obtain legal advice before they enter into any transaction that might be considered self-dealing or would involve a conflict of interest.

Any breach of this duty can be avoided by following the directions in the trust and by using common sense when dealing with its beneficiaries, making investments, distributing income or principal, etc.

Adhering to this general duty of care is particularly important whenever the trustee exercises any discretionary powers because those are the times when the trustee's impartiality and loyalty are most often questioned.

Successor Trustees

When your Trustee is no longer able and willing to serve in this capacity, a Successor Trustee must take over. All Trustees who follow you, have a job that is somewhat different from your role as a trustee, and their duties as a fiduciary are stricter. As the creator of your trust, your power to amend and revoke the trust allow you unique latitude in your role as trustee that no other person serving as your trustee may have.

Keep this in mind when you nominate successors. They have bigger shoes to fill!