

MEMORANDUM

TO: Trustees
FROM: James K. Leese
RE: List of Statutory Duties of Trustee

A "trust" is often described as any arrangement in which property (the "trust estate") is transferred by someone (the "settlor") to another person (the "trustee") for the benefit of a third person (the "beneficiary"). Trusts have existed for hundreds of years in England and the United States, originally being used to place an adult in charge of property which had been inherited by a child who was too young to manage his/her own affairs. Over the centuries, rules have developed which impose duties on persons acting as trustees. In 1986, the California legislature enacted statutes which list many of those duties. Trustees should be particularly aware of the following:

Probate Code Section 16000: Duty to administer trust. This statute requires the trustee to administer a trust according to law and in accordance with the trust instrument. No matter how good the trustee's intentions, the trustee is not free to administer the trust in some other manner.

Probate Code Section 16002: Duty of loyalty. This statute states that the trustee has a duty to administer the trust solely in the interest of the beneficiaries. The trustee cannot use the trust for his or her own benefit.

Probate Code Section 16003: Duty to deal impartially with beneficiaries. This statute states: "If a trust has two or more beneficiaries, the trustee has a duty to deal impartially with them." A trustee cannot favor one beneficiary over another. This is particularly critical when the trustee is also one of the beneficiaries. In such cases, it is a clear violation of the law for the trustee to favor himself or herself over another beneficiary.

Probate Code Section 16004: Duty to avoid conflict of interest. This statute requires that trustees avoid conflicts of interest. This prohibits a trustee from entering into transactions with trust property which will result in a profit to the trustee, or in which the trustee's interest is adverse to the interests of the trust or its beneficiaries. For example, a trustee usually must avoid loaning personal funds to a trust, because it would result in the trustee having a conflict between his duties to the trust and his duties to himself.

Probate Code Section 16006: Duty to take control of and preserve trust property. This statute requires trustees to take affirmative action to take and keep control of trust property and to preserve that property.

Probate Code Section 16007: Duty to make trust property productive. This statute requires a trustee to make property productive. This generally requires that the trustee make sure that property is wisely invested.

Probate Code Section 16009: Duty to keep trust property separate and identified. This statute requires a trustee to keep trust property separate from property not subject to the trust. For example, a trustee should not keep personal funds and trust funds in the same bank account.

Probate Code Section 16060-16061.9: Trustee's general duty to report information to beneficiaries. This statute requires trustees to keep beneficiaries informed with respect to matters involving the trust.

Probate Code Section 16062: Duty to account to beneficiaries. This statute requires trustees to provide beneficiaries with "accounts." Accounts are detailed statements regarding the financial transactions of the trust. They are similar to bank account statements in which a bank reports a "beginning balance," an "ending balance," and all the transactions that occurred during the reporting period that "account" for the difference between the beginning balance and ending balance. A trustee must keep careful records in order to be able to comply with this requirement.

Probate Code Section 16080: Discretionary powers to be exercised reasonably. This statute states that, when a trustee is given "discretion" with respect to a matter, the "discretion" must be exercised in a reasonable manner. The trustee is not free to act in whatever way the trustee wants. This is true even if the trust documents state that the trustee's discretion is "absolute" or "uncontrolled."

Probate Code Section 16200: General powers of trustee. A trustee's power (legal authority) to take actions pertaining to the trust is not unlimited, and in some cases may be very restricted. For example, a trust instrument may limit the kinds of investments which the trustee can make with trust property. This statute provides the trustee powers of those conferred by the statute and the trust instrument. Trustees must be careful to avoid taking unauthorized actions.

TRUST ADMINISTRATION PROCESS

Whenever someone passes away, whether or not an attorney will be retained to do the work, an attorney should be consulted to review the matter.

The following is a general summary of FERRUZZO & FERRUZZO, LLP's trust administration process, so that our clients will understand the trust administration process better. It was not written to give legal advice or to assist people who are trying to settle the trust without an attorney.

1. **Notice to Beneficiaries and Heirs**: As of January 1, 1998, the law requires us to notice all beneficiaries of the trust and the heirs of the decedent (whether or not they are named as beneficiaries of the trust) as to the fact that the decedent had a trust which is now irrevocable. The law also requires that beneficiaries be provided with a copy of the trust if they request it. Please advise us if you are aware of any heirs who were not named in the trust as a beneficiary.

2. **Notice to Director of Health Services**: Written notice to the Director of Health Services will be given, as required by law.

3. **Will**: Even though there is no probate, it is required by law that the original will is filed with the Court for safekeeping. We will file it and obtain certified copies of the will for you, if necessary.

4. **Inventory and Appraisal**: A comprehensive and precise inventory of all assets will be prepared. All assets will be appraised as of the date of death. The inventory will include non-trust assets as well as assets owned by the trust.

This step is crucial (and usually the most time consuming) because it will allow the attorney to:

- Determine how each asset must be transferred to the heirs.
- Determine who is to receive each asset.
- Determine how much estate tax is due, if any.
- Determine new depreciation schedule on income property.
- Do an asset split for an A-B Trust or A-B-C Trust.
- Document the stepped-up basis.
- Have a starting point for an accounting, if necessary.

5. **Asset split (for A-B and A-B-C Trusts only)**: After the inventory is complete, I will meet with you and the CPA to discuss which assets will be placed in Trust B (and C). There are many factors that need to be reviewed before deciding which assets will be placed in the sub-trusts.

Schedules will be prepared to show what assets are placed in the A Trust and what assets are placed in the B (and C) Trust(s). This is a very important step, because all assets placed in Trust B will never pay federal estate tax, so it must be clear exactly which assets are in Trust B.

If the trust is a Disclaimer A-B Trust, the disclaimer must be made within nine (9) months of the date of death or the decedent's estate tax exemption will be lost.

6. **Estate taxes**: If the decedent's estate exceeds the federal estate tax exemption, a Federal Estate Tax Return (Form 706) must be filed, whether or not there is tax due. The 706 and any tax due is due nine months from the date of death. An extension can be (and often is) requested, however, **THERE IS NO EXTENSION AVAILABLE FOR THE PAYMENT OF ESTIMATED TAXES.**

All assets passing to a surviving spouse qualify for the marital deduction and are federal estate tax free, if the surviving spouse is a citizen of the United States.

All assets passing to a non-spouse (i.e. a trust, the children, friends, etc.) or to a spouse who is not a United States citizen are exposed to federal estate tax. Assets under the federal estate tax exemption are exempt. All assets over the exemption are taxed at 37% to 49%.

7. **Income taxes**: Final tax returns for the decedent should be prepared and filed reporting the income earned up to the date of death. All income earned after the date of death should be reported on a Fiduciary Income Tax Return (Form 1041). FERRUZZO & FERRUZZO, LLP's does not prepare income tax returns, so you should consult your CPA as soon as possible. If your CPA has any questions, he or she should contact me.

8. **Trustee's Report (for Single Trusts only)**: Unless your beneficiaries waive it, you are required to give a full accounting of all of the income and expenses from the date of death to date of distribution. Let us know right away if you think the beneficiaries will waive their right to the accounting. If so, we will immediately prepare waivers for them to sign.

If you think the beneficiaries will want an accounting, you will be required to advise us monthly of all trust expenditures and receipts. Forms for this have been provided for you at the back of this book. If you have any questions about this process, contact the paralegal immediately.

9. **Transfer of Trust Assets:** To transfer real property, an affidavit of death and quitclaim deed will be recorded. To transfer deeds of trust, partnership interests, land sale contracts, etc., an assignment will be recorded or presented. To transfer bank accounts, stock, bonds, etc., an instruction letter will be mailed.

If there are any firearms in the estate, it is extremely important that you advise us immediately. In recent years, the federal government has outlawed many firearms that previously were typically owned by collectors. Your possession or transfer attempts of them could be unlawful or even felonious.

Assets must be transferred, even if the assets are merely going to a surviving spouse.

If you wish to sell or dispose of a major asset, please advise us of your plans prior to the sale. There may be tax or legal ramifications to the transaction which should be considered.

10. **Distribution:** Please Make No Distributions until you have discussed them with me. This is true even if you are the sole beneficiary. In the case of multiple beneficiaries, the general rule is that no distributions can be made until all debts and taxes have at least been assessed, if not paid. Advance distributions are strongly discouraged. This is for your protection.

Along these lines, please do not sell or acquire major assets without first notifying me. Sometimes these actions have tax implications.

11. **Your Responsibilities and Liabilities:** Even if you are one of the trustors, you bear responsibility and personal liability in your position as trustee. You are responsible to provide me with all information that you have about trust matters. This includes your knowledge of all trust assets and trust liabilities. Something to keep in mind is that you bear personal responsibility for all debts and all taxes if you do not see to it that they are paid from the trust assets in a timely fashion.

If you are one of the trustors, there is often a tendency to think of the entire trust as belonging to you. From a legal and tax standpoint, you need to shift your thinking. The survivor's trust is yours, but the exemption trust (and the QTIP trust, if there is one) does not belong to you. Your trust no doubt gives you some access to these sub-trusts, but they belong to the ultimate beneficiaries.

Whether or not you are also a trustor, in addition to the payment of taxes and debts as described above, as the trustee of the trust, it is your duty to do the following:

1. Protect and preserve the assets.
2. You have an affirmative duty to see to it that the trust assets grow and produce income.

3. You must invest the assets in a reasonable and prudent manner.
4. You cannot favor one beneficiary over another.
5. You must act in a timely manner. Do not engage in activity that will unduly delay the trust settlement and distribution. This is true, even if you are one of the trustors. Failure to make the trust split (in A-B or QTIP trusts) in a timely manner could adversely affect the tax liability of the estate should something happen to you before the split is made. Also, delay in making the split could adversely affect how the split is made.

Failure to meet these duties can result in your removal as trustee, even if you are one of the trustors.

The Uniform Prudent Investor Act clearly encourages a trustee to engage in appropriate delegation to qualified professionals. This policy should be adopted in order to reduce your potential exposure for unsuccessful investment decisions. A trustee who fails to seek advice with respect to matters about which the trustee lacks skill or knowledge may be liable for failure to exercise proper care in making an investment.

12. **Trust settlement team:** The attorneys and paralegals in our group will serve you as a team. I am personally responsible to you even though another attorney or paralegal is responsible for administration of the file and keeping it moving on a day-to-day basis. We think communication is very important so always call us if you have any questions or problems that you would like to discuss.

You will be kept posted of the progress throughout the case. Feel free to call us at any time to discuss the status of your trust settlement.