

# **FPA of Central Ohio Symposium**

## **Duties of Individual Trustees**

October 25, 2018

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# Introduction

- ➔ Importance of utilizing trusts and selection of trustees
- ➔ Revocable trusts
- ➔ Duties of trustees
- ➔ Protection for trustees
- ➔ Trustee fees

# Importance of Utilizing Trusts

- ➔ Avoiding probate
- ➔ Protecting assets
  - ➔ From a beneficiary's creditors
  - ➔ From a beneficiary's bad decisions
  - ➔ From a beneficiary's spouse (including a surviving spouse/beneficiary's subsequent marriage)
- ➔ From the grantor's creditors
- ➔ Minimizing estate/generation skipping taxes
  - ➔ Using GST exemptions
- ➔ Income tax planning

# Trustee Selection

- ➔ Institutions
- ➔ Individuals
  - ➔ Relatives of the grantor
  - ➔ Friends of the grantor
  - ➔ The beneficiary himself/herself
    - ➔ Beware of possible adverse income/estate tax consequences
- ➔ Power of others (e.g. beneficiary) to remove and replace a trustee
- ➔ Qualifications of individual trustees

# Revocable Trusts

- ➔ During the lifetime of the settlor of a revocable trust, the duties of the trustee are owed exclusively to the settlor. ORC 5806.03
- ➔ Coordination of successor trustee provisions and power of attorney upon settlor's incapacitation
  - ➔ Agent under power of attorney does not have authority to act on behalf of settlor to revoke, amend, etc. unless trust and power of attorney specifically authorize action

# Trustee's Duties: General Responsibilities

- Upon acceptance of trusteeship, the trustee shall administer the trust in good faith, in accordance with its terms and purposes and the interests of the beneficiaries and the code. ORC 5808.01
  - Keep trust accounts separate; do not commingle assets
  - Don't use assets for trustee's own benefit
  - Act in the best interests of the beneficiaries and treat them the same
  - Follow the trust terms
  - Invest assets in prudent manner
  - Keep accurate records, file tax returns and follow reporting requirements
  - Seek professional advice as needed to comply with prudent person standard

# Trustee's Duties: Duty of Loyalty

- ➔ A trustee shall administer the trust solely in the interests of the beneficiaries. ORC 5808.02(A)
- ➔ Except in discrete circumstances, the trustee is strictly prohibited from engaging in transactions that involve self-dealing or that otherwise involve or create conflict between the trustee's fiduciary duties and personal interests.  
Restatement (Third) of Trusts

# Trustee's Duties:

## Duty to Act as Prudent Person/Investor

- ➔ A trustee shall administer the trust as a prudent person would and shall consider the purposes, terms, distributional requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill and caution. ORC 5808.04
- ➔ A trustee shall invest and manage assets as a prudent investor would, by considering the purposes, terms, distribution requirements and other circumstances of the trust. In satisfying this requirement, the trustee shall exercise reasonable care, skill and caution. ORC 5809.02

# Trustee's Duties: Duty of Impartiality

- ➔ If a trust has two or more beneficiaries, the trustee shall act impartially in investing, managing, and distributing the trust property, giving due regard to the beneficiaries' respective interests. ORC 5808.03
- ➔ Comment from the UTC: “[t]he duty to act impartially does not mean that the trustee must treat the beneficiaries equally. Rather, the trustee must treat the beneficiaries equitably in light of the purposes and terms of the trust.”

# Trustee's Duties: Duty to Inform and Report

- ➔ A trustee shall keep the current beneficiaries of the trust reasonably informed about the administration of the trust and of the material facts necessary for them to protect their interests. ORC 5808.13
- ➔ Trustee, on its own initiative (without request by beneficiaries) must:
  - ➔ Provide notice to current beneficiaries of the existence of an irrevocable trust or a revocable trust becoming irrevocable. ORC 5808.13(B)(3)
  - ➔ Provide notice to the current beneficiaries of the identity and contact information of the trustee and any changes in trusteeship. ORC 5808.13(B)(2)
  - ➔ Provide an annual report to the current beneficiaries. ORC 5808.13(C)
- ➔ Trustee has a duty to respond to a beneficiary's request for reports and other information reasonably related to the administration of an irrevocable trust. ORC 5808.13(A)

# Trustee's Duties: Communication

## *Zimmerman v. Patricia E. Zirpolo Trust*

- ➔ Parent of three minor trust beneficiaries filed suit on behalf of the minor beneficiaries against individual trustee seeking a copy of the trust instrument and an accounting.
- ➔ Trial court denied mother's request on grounds that settlor's intent clearly stated that beneficiaries were not entitled to information regarding the trust until they reached age 35. Mother appealed. Ohio Court of Appeals reversed and remanded. Trial Court again denied request. Mother again appealed.
- ➔ Ohio Court of Appeals held that the Ohio Trust Code's provisions requiring a trustee to furnish a copy of the trust to a beneficiary upon request and to keep beneficiaries reasonable informed takes precedence over the settlor's intent. Accordingly, trustee had a duty to provide the requested documents to Mother as the representative of the minor beneficiaries.

Zimmerman v. Patricia E. Zirpolo Trust, 2012 Ohio 346 (Ohio Ct. App. 2012)

# Trustee's Duties: Communication and Duty of Impartiality Restatement of Trust Illustration

- ➔ Trust is a broadly discretionary trust for the benefit of grantor's widow (W) and descendants.
- ➔ Trust terms make it clear that W is the primary beneficiary; however, distributions can be made to any one or more of W and descendants.
- ➔ The children (A, B, and C) are adults. C is estranged from family and Trustee is aware of estrangement.
- ➔ Trustee keeps W, A and B well informed of trust affairs and meets with them periodically to discuss their needs.

# Trustee's Duties: Communication and Duty of Impartiality Restatement of Trust Illustration (Cont'd.)

- ➔ Due to the financial security of W, A and B, no distributions are made except to sprinkle income to A, B and C (and their children) to minimize income taxes.
- ➔ Trustee sends C her annual distribution with required tax information but has no other communication with her.
- ➔ C, who has financial needs, knows nothing about the trust except that it was established by her father, and her mother is the primary beneficiary.
- ➔ Trustee is violating the duty of impartiality by not communicating with C facts necessary to protect her interests as a beneficiary.

# Irrevocable Life Insurance Trusts (ILITs)

- Unless the terms of the trust provide otherwise, the duties of a trustee with respect to the acquisition, retention, or ownership of a life insurance policy as a trust asset do not include any of the following duties (ORC 5809.031):
  - To determine whether the policy is or remains a proper investment
  - To diversify the investment in the policy relative to any other life insurance policies or trust assets
  - To pay policy premiums, unless there is sufficient cash or other readily marketable trust assets from which to pay the premiums or there are other trust assets designated to be used for payment of premiums
  - To investigate the financial strength of the life insurance company maintaining the policy
  - To inquire about changes in health or financial condition of the insured under the policy
- Contributions to ILITs are not considered present interest gifts unless beneficiary has actual notice of the withdrawal right and reasonable time to exercise the right (Rev. Rul. 81-7)

# Protection for Trustees: Ohio Revised Code

- ➔ Trustees can use judicial proceeding to resolve various issues or potential disputes arising from trust administration. Trustee can seek court guidance on any matter involving the administration of a trust. ORC 5802.01.
- ➔ Absent a breach of trust, a trustee is not accountable to a beneficiary for profit made by the trustee arising from trust administration. ORC 5810.03(A)
- ➔ Absent a breach of trust, a trustee is not liable to a beneficiary for a loss or depreciation in the value of trust property or for not having made a profit. ORC 5810.03(B)

# Protection for Trustees: Consents and Releases

- ➔ A trustee is not liable to a beneficiary for breach of trust or breach of fiduciary duty if:
  - ➔ The beneficiary consented to the conduct;
  - ➔ The beneficiary released the trustee from liability; or
  - ➔ The beneficiary ratified the conduct. (ORC 5810.09)
- ➔ Requirements for a valid release:
  - ➔ Cannot be induced by improper conduct of Trustee;
  - ➔ Beneficiary must be aware of his or her rights;
  - ➔ Beneficiary must be aware of all material facts; and
  - ➔ There must be consideration for the release.

# Protection for Trustees: Consents and Releases (cont'd)

- ➔ Impact of consent and release
  - ➔ If no release is obtained, beneficiaries have 4 years to bring an action against a trustee for matters pertaining to trust administration. An effective release bars a beneficiary claim even during this period of time.
- ➔ When an individual trustee should consider asking for a consent and release
  - ➔ Beneficiary requesting action that isn't explicitly permitted under trust
  - ➔ It is unclear from trust language whether requested action is permitted
  - ➔ Trustee is resigning
  - ➔ Final trust distribution is being made
  - ➔ Release is advisable to mitigate risk due to likelihood of beneficiary dispute

# Protection for Trustees: Distributions

- ➔ Receipt & refund agreement for distributions made during estate administration
- ➔ Special procedure for trust termination ORC 5808.17
  - ➔ Trustee of terminating or partially terminating trust may send a proposal of distribution to the beneficiaries
  - ➔ Beneficiary's right to object to proposed distribution terminates 30 days after receiving proposal

# Protection for Trustees: Exoneration by Trust Instrument

- ➔ It is common for trust instruments to relieve trustees from liability for any act or failure to act so long as the trustee was acting in good faith.
- ➔ Provisions in trust instrument relieving a trustee of liability for breach of trust are generally enforceable.
- ➔ However, such a provision is unenforceable to the extent it relieves the trustee of liability for a breach of trust committed in bad faith or with reckless indifference to the purpose of the trust or interests of the beneficiaries. ORC 5810.08.

# Protection for Trustees: Delegation

- ➔ A trustee may delegate investment and management functions of a trust that a prudent trustee having comparable skills could properly delegate. ORC 5809.06(A)
- ➔ A trustee who delegates a function to an agent is not liable to the beneficiaries of the trust for decisions or actions of the agent to whom the function was delegated. 5809.06(C)

# Protection for Trustees: E&O Insurance

- ➔ We advise individual trustees, especially non-relative trustees, to acquire E&O coverage
- ➔ Consider indemnification provisions in trust agreement

# Trustees Fees

- ➔ Trustee compensated according to terms of the trust. However, court may allow more or less compensation. ORC 5807.08(B)
- ➔ If terms of the trust do not specify trustee compensation, trustee is entitled to compensation that is reasonable under the circumstances. ORC 5807.08(A)

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## Questions?

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