THOUGHTS ON HOW TO STRUCTURE A TRUST

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I have conversations with clients about estate planning, and the topic of Trusts invariably comes up. Trusts can be good solutions to specific problems, but they can be expensive and complicated solutions to problems that have easy, inexpensive solutions. Trusts are used to leave money to people you do not trust—right now—to take care of your hard-earned assets. To know whether a Trust is the solution to your problem, we start by defining the problem (or problems) the Trust is intended to solve through a series of questions.

Are you worried about what the heirs will do with an inheritance? Are you afraid it will be spent on wine, women, and song? Political or charitable contributions to causes you do not approve of? Something worse? What are you willing to spend in terms of time, energy, and money to keep those things from happening? And if it really bothers you, then why leave the heirs anything at all? I bet you know several worthy causes you could support.

While you are alive your assets should provide spending money to last the rest of your life. What do you hope will happen to your money after you are gone? What are you trying to ACCOMPLISH?

These are important questions. Think about your answers and write them down.

Let us say your goal is to provide your heirs with money to cover basic necessities. You also want to provide incentives to work, save, and invest for themselves, but you worry they will blow through the money. To prevent that from happening, and to provide a lifetime financial “cushion,” establishing a Trust makes sense.

Think about what you want, refine it, and write it down until what you are trying to accomplish is clear and concise. Then go to a lawyer and talk about a Trust. The specifics of each Trust are different, but here are my suggestions for general requirements:

1. The Trust needs a Statement of Investment Policy that incorporates the multi-year/multi-decade life of the Trust and the effects of taxes, fees, and inflation on the purchasing power of the Trust assets.

2. The Trust should be specific about the purpose and desired outcomes for the Trust and flexible and adaptable as to how it achieves the Trust objectives. References to providing “income” should be replaced with generating a “cash flow” to the beneficiary, and that cash flow should be capped at 4-5% of the three-year trailing average of the market values of the Trust. The Trustee should have the power to exceed that cap under what they determine to be extraordinary circumstances (which you can spell out in the Trust.) The Trust is designed to last for decades, and it MUST be able to adapt to changing economic, market, political, and social conditions. DO NOT specify certain stocks for the Trust to own, or asset classes, or investment types (the place for that is in the Statement of Investment Policy, which can be incorporated into the Trust by reference.)

3. There are four distinct roles in a Trust like this: The Settlor (that is you), the Beneficiary (that is you initially, then your heirs/charities), the Trustee(s) (that is you initially, then a successor trustee), and the Investment Advisor(s). Trustees and Investment Advisors should be independent, and a mechanism for replacing one or both is needed. You can have more than one of each, but I suggest reasonable limits. Two co-trustees, one private individual trustee and one corporate trustee, can be useful. More than three Investment Advisors can be counter- productive (and they should ALL be subject to the same Investment Policy).

4. Combined fees for the Trustee and the Investment Advisor should stay below 1.5% of the Trust Assets per annum. Taxes, inflation, and FEES will shrink the purchasing power of the Trust Assets; the investment performance must be greater than or equal to the sum of those items.

Those are the primary points. I suggest taking everything you have written down—**goals, problems, investment policy**, etc.—to a lawyer when you meet with them. Once they have drafted the Trust, make sure you can identify where **each one** of your items is located in the Trust. You should also ask about the sections in the Trust that do NOT address your items. Why are they there?

Following this outline will help you KNOW what you want to accomplish, why, and how the Trust document executes that plan.