

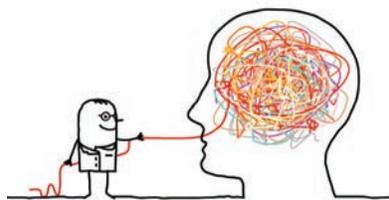
tends to look like this: “My trustee shall invade principal for my spouse for health, education, support and maintenance.” We call this “IRS-sanctioned ascertainable standards,” and this means that if you use this language the surviving spouse can be trustee without adverse tax consequences. If you want less restrictive language, a disinterested trustee such as the Trust Company of Vermont may be needed.

Whether you should consider using your spouse as trustee of your trust for his or her benefit after you are gone depends on whether he or she will stay inside the box and is adequately protected by an infrastructure (see next page) that will provide informed guidance as to the parameters. I am reminded of a story about an acquaintance who was designated trustee of her spouse’s tax savings trust. She called her broker and said she needed \$100,000 to simply add to her checking account. He sent it to her, no questions asked, even though he knew the purpose of the trust. Absent a process of substantiating and documenting compliance with the principal invasion clause, this transaction was a violation of her fiduciary duties, which may have a negative impact in the future. The IRS does not like you stepping out of the box. And in some instances, neither will the recipients of the trust, upon termination.

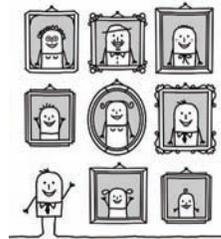
THE BOX FOR CHILDREN

“*In Loco Parentis*” takes me back to college when a shift occurred to control my behavior. The College was now my parent. We have many trusts where we act in a similar capacity. And now the box becomes very important.

Estate planning can be daunting. Sometimes in the process one can get distracted and not focus on the boxes for children or others whom we need to care for until they are able to handle their own finances. For some children, this may be a challenge that will last a lifetime. To be sure, we have a number of trusts for children where the principal objective is tax savings, and the invasion clauses are designed primarily



to accomplish this objective. Those boxes tend not to be customized. One of the challenges in estate planning is to customize the boxes when a trust is necessary for children for non-tax reasons.



In our July 2010 newsletter we expressed our *per stirpes* preference. That is, we favor treating all the children the same in terms of how much of your estate they will receive. That said, we think that some children’s shares should be held in trust and others should be paid outright, depending on the needs, capacity, personality, circumstances and all those other factors that you would consider were you still alive.

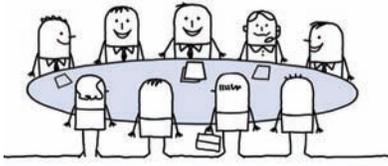
You can have principal invasion standards that are very broad. If you do, don’t have a single fund for all the children, or have a way to adjust shares for a principal invasion that favors one child over another. Without standards it is very hard for the trustee to invade principal for one child knowing that the other children’s share will be reduced proportionately.

When designing the principal invasion box, here are a few things to think about: should you include standards related to health, education, support and maintenance; support for spouses; support for grandchildren; principal to buy a home or start a business, to name a few?

If you decide that you would like one of the siblings to act as trustee, just be mindful that if this responsibility puts the child in an awkward position, you may want to consider a disinterested co-trustee who can make the invasion decision alone if so authorized. The important thing is to take time to think into the future in designing the box. This box may have a profound effect on your future generations.

THE TRUST COMMITTEE

When we receive a request to invade principal or increase a discretionary income distribution above \$1,500, the administrator brings the request to a committee. Last year the Committee deliberated 53 times.

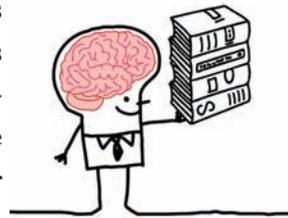


Why a committee? It is our experience that we need multiple personality types to make the best decision.

To be sure, the meeting is dominated by the convergent thinkers, but we also have at least one divergent thinker present. Sometimes we need to spend time exploring the parameters. I think often of a request from a 33-year old beneficiary for funds to provide for a house down payment. A reasonable request from a responsible person but the trust only provided for a distribution to her when she was 35 and did not authorize us to invade principal. We loaned her the down payment and gave her the note when she turned 35. A divergent thinker found authority for us to make a personal loan. Sometimes boxes can be larger than they first appear ~ but they are boxes nonetheless. That's why it's good to think about the trustee's discretion to act when you are not around.

TRUST INFRASTRUCTURE

If one uses family or friends as trustees of irrevocable trusts they should have a support network. This network should include investment managers familiar with fiduciary obligations, individuals knowledgeable in fiduciary accounting and fiduciary tax accounting (they are not the same) as well as fiduciary tax preparation, and perhaps a lawyer on call. They also will need to use a transaction accounting system that will separate receipts and disbursements into columns marked principal or income.



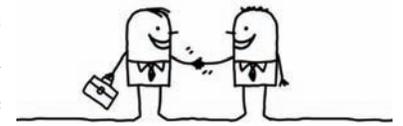
The Trust Company of Vermont furnishes such a service and we have seen a growing trend to use family members as trustees. Whereas years ago we would be trustee of almost all our irrevocable trusts, now approximately a third are accounts where we simply furnish the infrastructure.

BREAKING THE BOX

Sometimes a trust will neglect to include important provisions. I am reminded of an instance at the Vermont National Bank Trust Department concerning two trust officers and a trust with a very big hole in it. Years

ago, bank trust departments often agreed to act as trustee for very small trusts and some of these trusts, drafted before the word processor, were models of brevity. The bank was administering one such trust set up by a retired school teacher for the educational benefit of a promising student. The trust provided for distributions to pay for the student's college education. The trust did not address the possibility that the student would not go on to college nor did it provide for a termination date or remainder beneficiaries. The student left high school, went into the service, and upon his return applied to the bank trustee for funds to go to a TV repair school. The trust officer ~ let's call him "Bill" ~ was new and knew only how to deny with a perfunctory "No, doesn't meet the standard."

He never heard from the student again. More than twenty years passed. Then one day Bill noticed the trust, and by this time understood that a "No" should be accompanied by a guide ~ not simply denied. So he turned to a colleague and asked if she could help find the student, now well past his college years. "Sue" hired a detective agency and found him one town over. The student had not gone to college and was a tradesman. Knowing this, Bill suggested that Sue call and find out if he had children in college. If so, she could volunteer the trust assets even though the trust did not specifically authorize this expenditure. The trust was simply too small to afford the costs of court authorization. Sue called. The man had gone to bed literally the night before, praying that he could find a way to afford college for his daughter. Sue and Bill broke the box. The daughter went to college. Sue took the credit and the "denied" beneficiary still hates Bill. But Bill feels better now.



In Vermont there is an active group of trust officers and attorneys working to modernize our trust law. Recently this group was responsible for passage of the new Vermont Trust Code ("VTC"). The VTC has many important parts to it, including the ability of the Probate Court to modify all trusts that need to be updated. Some of us in the trust field find the above story, although true and perhaps heart-warming, somewhat troubling in that trust officers shouldn't be filling in the blanks. If a box needs to be changed or added, we now have a speedy and inexpensive way to do it. Our own Christopher Chapman is part of this group and in our next issue he will be discussing some of the most recent changes.