

Three examples of living trusts

Sound financial planning has always been important, and it has always been challenging. There are many crucial and difficult elements to financial planning, coming under headings such as investment selection, total rate of return, risk analysis and meticulous recordkeeping. There must be a skilled leader, orchestrating the efforts of many other skilled professionals, working together to implement a carefully developed plan.

The essence of the *core* challenge is to be prepared for both anticipated needs and unexpected developments. Being prepared means, in substantial part, having selected a financial plan leader who can react flexibly as circumstances change.

Here are three realistic examples from our files, fictionalized to protect the privacy of our clients, that illustrate the practical problems financial plans must address. Investment factors, fundamental analysis, portfolio balance, tax decisions and risk tolerance are each important plan elements also, but we omit them from this discussion. Instead, we focus on the larger themes of control, flexibility and judgment.

Protection during disability

Consider a fictitious retired couple, John and Martha Ross, who are living quite comfortably on their investment assets, Social Security benefits and John's pension. John has handled the investment details, collecting interest and dividend income and making occasional trading decisions. The Rosses aren't pursuing capital growth, just a steady and reliable income stream.

John is the older of the two, and his health is only fair, as one would expect. The Rosses need to be prepared for several possibilities.

What if something happens to John, requiring an extensive hospital stay? Who will take over managing the investment portfolio? What if he becomes mentally disabled, unable to continue his financial management responsibilities? What if something suddenly happens to Martha? John's attention necessarily will be diverted to her needs and taking care of the household, again at the expense of adequate supervision of the family's finances.

To be prepared better to manage these possibilities, the Rosses established a trust. The trust contains their investment assets, which we keep organized and manage on their behalf. Currently, we do not make any buy or sell decisions; we simply deposit investment income in the Rosses' checking account.

But should an emergency arise, the trust instrument authorizes us to take full investment control, upon notification by either John or Martha of the need. There will be no financial disruption; we even are authorized to pay medical bills as necessary.

The couple's wills also have been linked to this trust. Should John die first, insurance proceeds on his life will flow into the trust to provide consolidated and comprehensive management on Martha's behalf. Because the trust is in place now and operating smoothly, death will not create the financial havoc for the survivor that otherwise could ensue.

Privacy

Sylvia Henley-Davis (this name, of course, is also fictitious) is a well-known, wealthy person, almost a public figure. In fact, much to her distress, she once found her picture in one of the sensational tabloids that traffic in racy gossip.

Sylvia plans to leave a large part of her wealth to a number of businesses and social acquaintances, persons who are not related to her. She doesn't want this fact ever to become public; she is afraid of creating embarrassment for the beneficiaries and, perhaps, for her family. Sylvia also is concerned that certain nephews of hers might attack her will in court.

Sylvia has established a trust for herself, just as the Rosses did. As trustee, we are actively supervising the management of the trust assets, in accordance with a plan that we developed with Sylvia and her financial advisers. The trust substitutes, in part, for Sylvia's will; it provides that at Sylvia's death set percentages of the trust will be transferred to named beneficiaries, and the balance will go to a charitable foundation.

When Sylvia dies, the terms of her will must become public knowledge, as the will is filed with the probate court. The terms of the trust, however, never will become public; no one but the trustee and the beneficiaries will be aware of the ultimate disposition of the trust assets.

Should the nephews try to attack the trust in court, they have a much lower chance of success. A challenge to a will is typically based upon what the will's maker really intended. Since the trust operated with Sylvia's approval during her life, it is clear that she intended its terms to be carried out.

The importance of privacy is by no means limited to public figures. People who suddenly come into money often are besieged by con artists and "old friends," as well as by legitimate vendors of financial services—as press reports about lottery winners attest. A trust helps eliminate publicity at a time when a family most desires privacy and solitude.

Structured control

Samuel Cooper (the name is fictitious) is the patriarch of a very successful family business. His children have also met with success in life, some in his business and others not. He attributes their successes in part to the fact that his own financial rewards came late in his life; the children were not spoiled by money.

Now Samuel is wondering how he might best share his fortune with his grandchildren. He wants to give each of them enough of a financial base to give them a strong start in life, but he doesn't want to make the base so large as to sap their drive. He has a horror of the "idle rich." In fact, Samuel wants to use his wealth to pique their ambition.

Yet Samuel can't know today which of his descendants will prove worthy of his generosity, who will respond positively to incentives he wants to create.

The trust that Samuel established includes a number of separate provisions. Each grandchild will receive financial assistance from the trust for both undergraduate and graduate studies. Then, upon employment, each grandchild will receive from the trust an amount equal to one-half his annual earned income, up to a maximum of \$30,000—in effect, a reverse income tax.

Each grandchild also will own a 5% share of the total trust assets. One-third of that share will be distributed to the grandchild upon reaching age 30, provided the grandchild has become a responsible member of the community. The remaining two-thirds will be distributed when he or she reaches age 40.

Trial run: Samuel could have set this trust up in his will. He didn't for two key reasons. First, he wanted the terms kept private. And second, frankly, he needed to be sold on making us the investment manager. We are being put to the test today; we are proving our leadership abilities and establishing a performance record for his trust. If Samuel is dissatisfied, he may change trustees or cancel the entire arrangement.

This point applies equally to each of the examples we've outlined. Each trust was revocable, so the person making the trust never gave up ultimate control of the financial plan. Yet each added players to the financial management team—our staff of highly trained experts. This strengthened the total financial plan by adding expertise, flexibility, an independent viewpoint and uninterrupted management.

Many persons include trusts in their wills, most commonly to protect a surviving spouse. But there is no need to wait to gain trust advantages. Once you learn how good we are at what we do, you will have gained the peace of mind regarding family financial security that is the ultimate objective of sound financial planning.

If a trust plan could work for you, call on one of our officers soon.

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