AGENCY and FIDUCIARY RESPONSIBILITY IN THE USE OF TRUSTS, WILLS, and PARTNERSHIPS

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Foreword

~ Agency and Fiduciary Responsibility ~

No area of the law is more widespread than "***Agency law***," affecting all but the most isolated recluse daily in a multitude of relations with other persons, often from dawn to dusk and beyond.

If one were a castaway on a desert island with no other inhabitants, there would be no need for *agency law*, or any other law for that matter. With the arrival of "my man Friday", a two-part ***P****rincipal* and ***A****gent* ("**P**-**A**") relationship was birthed. With the influx of Friday's people and opposing tribes, the typical three-part relationships involving the ***T****hird person* ("**P**-**A**-**T**") began.

As society has grown increasingly interdependent, with many new activities, *agency* relationships have become more prevalent, innovative, complex, and significant.

Agency can involve any power conferred by one person on another to do something for the former, usually requiring no formality and sometimes no express communication, and not necessarily any compensation or other consideration; in effect, when one person acts for another.

Agency law also comprises a large portion of partnership law, the other portion being the characteristics of that very common unincorporated business enterprise (i.e., partnerships, joint ventures, associations, business trusts, etc.), including many law and professional partnerships. By analogy, agency and partnership principles apply to countless unincorporated nonprofit associations.

Although *agents* are *fiduciaries*, not all *fiduciaries* are *agents*. Administrators, executors, guardians, receivers, trustees, and the sort are not appointed by, nor subject to, the control of those whom they

owe their *fiduciary* duties. However, because of contractual relationships that may exists between the above mentioned *agents* and their *subagents*, i.e., managers, banking agents, signatories, etc., these *subagents* become *fiduciaries* to the entities contracting them.

Besides employers (***p**rincipals*) and employees (***a**gents*); attorneys, doctors, accountants, architects, other professionals, brokers and other nonprofessionals (***t**hird persons*), with their clients, partners, associates, other employees, and correspondent out-of-state or country personnel; are all involved in *agency law*, and perhaps *fiduciary*. Also involved are travel agencies, their providers of goods and services, and clients; banks, including all those involved in the check collection process; corporate officers and other employees; shareholders and their proxy holders; service stations, whether owned, leased, or franchised by oil companies; car dealers in their sale of new cars, repairs, and purchase, repair, and sale of used cars; franchisors and their franchisees; lessees of equipment and their operators; and even newspaper carriers.

As expressed in the Latin maxim, "*Qui facit per alium facit per se*" (who acts through another acts oneself, i.e., the acts of the ***a**gent* are the acts of the ***p**rincipal*). This should not be taken literally. Only if the other person ("*alium*") is an ***a**gent* does the maxim usually apply.

Since this is a limitexd text on the inter-relationship between "*fiduciary responsibility*" and "*agency*"; it is appropriate that the substantive portion of the text begin with analysis of some of the characteristics of *fiduciary responsibility*. See Illustration 1-1.

In its simplest terms, *fiduciary responsibility* simply refers to the obligation imposed on an individual, or institution, who undertakes to perform services for the benefit of another where there exists a high degree of confidence in such an individual or institution and where the reliance is inherent in the establishment of the relationship. In this text, it first refers to a relationship between legal counsel and advisors in

the estate planning process in their responsibility to clients, and, second, to the responsibility placed on the individual or institution which would be functioning in formal capacity as a general partner, corporate officer, trustee or executor, or as any individual exercising powers on behalf of another.

An examination of Illustration 1-1 may help place the entire arrangement in context. Illustration 1-1 shows that even though the foundations of estate planning are efficient, well-drafted legal instruments, careful implementation, and an investment portfolio which will maximize the financial success of the family, all of these activities are covered by the *fiduciary responsibility* imposed upon all activities within this system. The responsibility extends not only to the documents per se, but also to implementation, reporting, and investment activities.

Fiduciary responsibility is not only the covering or roof of the house of quality estate planning; it is also the walls providing structural strength and context in which the process exists. In fact, the *fiduciary responsibility* should be perceived as the adhesive which must permeate all the components of quality estate planning to ensure that all activities, documents, and conduct are melded together as one whole.

Fiduciary Responsibilities in the Use of Trusts

Section 1.01 History of Concept

The concept of *fiduciary responsibility*[1] dates back to *fiducia* of Roman law as so explained in the Oxford English Dictionary (2d ed 1989). The concept under Roman law of *fiducia* denoted the transfer by an individual "holding a right of that right" to another who is to use "that right for the benefit of the person making the transfer," with the underlying understanding that "the right will at some point in the future be returned to the person making the grant of the right."

The entire concept was founded on concepts of trust, confidence, honesty, and integrity. The development of the term in legal history under the common law suggested a situation wherein a person assumed the character of a trustee, or an analogous relationship, where there was an underlying confidence involved that required scrupulous fidelity and honesty [**Stoll v. King, 8 How Pr 298 (NY 1953)**]. Early case law suggests this referred primarily to relationships concerning individuals and tangible property. The development of the concept of a *fiduciary* in the areas of relationships in corporations and partnerships indicates that it has expanded far beyond the simplicity of relationships wherein tangible property was involved. It now encompasses any relationship between individuals wherein there is imposed upon one individual the highest degree of fidelity that exists in the law.

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[1] **IRC § 7701(a)(6)** - "The term "*fiduciary*" means a guardian, trustee, executor, administrator, receiver, conservator, or any person acting in any *fiduciary* capacity for any person."

Section 1.02 A Proper Definition of Concept

Defining words is a nearly impossible task when the term is one which is conclusionary in nature. In most areas of the law, those words with significant meaning and which are particularly relevant to understanding the law are conclusionary. Such terms usually denote situations which come into existence by virtue of a series of events and an analysis of the conduct and relationships of parties. Hence, defining such words is difficult.

Defining of words per se can be categorized into four methods for analysis. An examination of these may be helpful in recognizing the complexity of attempting to define the term *fiduciary*.

Etymology-The History of the Word

The foundations of the term appear to come from the Latin *fiducia*, referring to ideas of trust or confidence. In theological terms it was expanded beyond trust, confidence, and reliance, to encompass both an intellectual and a faith component concerning confidence in divine promises. It is important to recognize that historically the word had its foundations to some degree in concepts relating to the divine. It is this foundation which imbues the concept with a high degree of "moral content," which may be unique in the history of legal concepts. It emphasizes that the essence of the concept is the imposition of responsibility on the individual acting as a *fiduciary*, the highest level of responsibility imposed on an individual acting in a legal context.

Although this definitional approach is not totally satisfactory, it is useful in analyzing the word in the law. It does help to lay the foundation to recognize the direction in which the concept has developed.

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Synonyms

Though synonyms seems to be the least useful way of defining such complicated concepts as *fiduciary*, those which seem most appropriate would include trust, reliance, confidence, fidelity, and integrity.

It is obvious these are words descriptive of the mental set of the individual who is relying on the individual acting in a *fiduciary* capacity, but they do not adequately describe the related conduct. Describing qualities of character or perception only helps lay the groundwork of definition. The result of an individual acting in a *fiduciary* capacity can only be meaningfully articulated in terms of conduct which demonstrates the reality of the characteristics.

Per Genus et Differentiam

Normally, the concept of definitions *per genus et differentiam* is a very useful technique. However, it is particularly inadequate in attempting to elucidate legal terms. There's a case that was decided in the state of Montana which evidences an attempt to define in these terms. The case suggests that the *fiduciary* is in a confidential relationship which is "founded on trust or confidence reposed by one person in the integrity and fidelity of another." [**Kerrigan v. O'Meara, 227 P 819 (Mt 1924)**; **Hodges v. Hodges, 692 SW2d 361 (Mo Ct App 1985)**]

Although this is a nice way of defining the term *fiduciary* in broad strokes and one which seems appropriate for this decision, it does not explain the various elements which are necessary before we can suggest that the *fiduciary* relationship in fact is imposed and has been fulfilled.

Conclusionary Definitions

This is perhaps the most satisfactory way of attempting to define or articulate a term which can only meaningfully be described by examining conduct of a person or institution, and analyzing whether that conduct is such as to reach a standard of having fulfilled a particular obligation.

In attempting an examination of conduct which will help the reader conclude whether there has been a *fiduciary responsibility* imposed, and whether it has been fulfilled, a number of cases will be examined. It may initially seem that there is significant overlap in many of these cases. This is clearly the case. But it is hoped that the cases chosen will each contribute a peculiar twist or clarification of a concept which will add to the final attempted conclusionary definition. It may well be that at times these distinctions are simple nuances, but attempts have been made to demonstrate the legitimacy of their use by textual interpretation.

Also, some cases have been used to demonstrate situations where conduct under a particular trust situation initially seemed to be without meaningful distinction. However, careful analysis of the cases will demonstrate that there is either a difference in conduct, or additional conduct, or an imposition of legal responsibility that makes the difference in a court's determining that under one particular situation, it would impose *fiduciary responsibility*, whereas in another, it would find it does not exist.

From those cases, it is hoped that a checklist of relevant questions can be derived, the results of which will help to suggest those situations in which the balance of the scales tips more clearly toward the imposition of the *fiduciary responsibility*.

By way of example, the North Carolina court in Hinshaw v. Wright held that "[i]n determining whether a person or entity is a '*fiduciary*,' examined function performed, rather than the title held." [**412 SE2d 138, 144 (NC Ct App 1992)**]

It is particularly relevant that the court should have used the term *function*, which is for all intents and purposes a verbal equivalent to conduct. Therefore, it is observed "actions" and "conduct" of the person which determines whether it can be concluded that the individual has fulfilled their *fiduciary responsibility*. The examination of that conduct may well be both positive and negative.

By way of example, in a South Dakota case, the court held that trading in commodities was imprudent per se. [***In re* Hyde Trust, 458 NW2d 802 (SD 1990)**] In the ruling the court held that simply engaging in commodity trading violated the "prudent man rule" and, hence, was a negligent violation of standards imposed on trustees. The court went further to observe that commodity trading was "inconsistent with the creation and maintenance of a trust" in that it failed to reasonably follow conduct which would preserve principal or produce income necessary to the estate.

In situations involving attorneys, the courts have consistently held him or her to be a *fiduciary* because the client reposes substantial confidence in him or her. Therefore, any conduct by the attorney which could lead to the client's disadvantage would clearly hold the attorney in breach of their *fiduciary responsibility*. Another court, in finding that an individual such as an attorney is per se a *fiduciary*, indicated that such an individual has the "burden of proving fairness and honesty of such transactions." [**Olds v. Hitzemann, 220 Ind 300, 42 NE2d 35, 37**]

Another court has defined the term *fiduciary* in even broader terms. Specifically the court has indicated that:

> [T]he term "*fiduciary*" applies to any person who occupies a position of particular confidence toward another. It refers to integrity and fidelity. It contemplates fair dealing and good faith, rather than legal obligation, as the basis of the transaction, and includes those informal relations which exist whenever one party trusts and relies upon another, as well as technical *fiduciary* relations. [**Kinzbach Tool Co v. Colbett-Wallace Corp, 138 Tex 565, 160 SW2d 509, 512** (9142)]

In a case concerning estate planning, an Illinois court has held:

> "Fiduciary" or "confidential" relation, as used in the law relative to undue influence, is a very broad term. It has been said that it exists and relief is granted in all cases in which influence has been acquired and abused, in which confidence has been reposed and betrayed. The origin of the confidence and the source of the influence are immaterial. The rule embraces both technical *fiduciary* relations, and those informal relations which exist wherever one man trusts in and relies on another. [**Thomas v. Whitney, 186 Ill 225, 57 NE 808, 810 (1990)**]

An individual with authority over the administration and management of funds for the benefit of others becomes a *fiduciary*, and, hence, has an affirmative obligation of proper record keeping and the dissemination of information to employees who are entitled to the benefits of such funds.

In a Minnesota case the court held that the controller exercised discretionary authority with respect to the administration or management of the retirement plan in question, and, thus, was

"*fiduciary*" with respect to that plan, where the controller worked on amendments made to the plan, was largely responsible for informing the employees about the plan, met with the employer's independent accountant to discuss issues of officially recognizing, for purposes of the plan, one-third bonus paid to management, consulted on the plan investments, and had authority to make some press releases without an officer's prior approval. [**Monson v. Century Mfg Co, 739 F2d 1293 (8th Cir 1984)**]

An Ohio court has declared: "A 'trustee' or '*fiduciary*' is not an ***a**gent*, and does not have any ***p**rincipal*, but is a person in whom there is vested, for benefit of another, some estate, interest, or power in or affecting property." [**Muth v. Maxton, 119 NE2d 162, 166 (Ohio CP 1954)**]

This is not to suggest that a ***p**rincipal* may not become a *fiduciary*. The thrust of this case is that being a ***p**rincipal* does not per se make an individual a *fiduciary*. Other cases have demonstrated that where the relationship of the ***p**rincipal* and ***a**gent* evolves into one of significant trust, then the ***a**gent* may become a *fiduciary*.

In an early New York case, the judge stated:

> The term "*fiduciary*," as I understand it, involves the idea of trust, confidence. It refers to the integrity - the fidelity of the party trusted, rather than his credit or ability. It contemplates good faith, rather than legal obligation, as the basis of the transaction. When an ***a**gent* or attorney is employed to collect money, he acts under a special trust. The money received is not his own. He holds it in a special trust, to pay it over to his ***p**rincipal*. Money received under such circumstances, is received "in a *fiduciary* capacity." The ***p**rincipal* has confided

in the man, rather than his ability to pay. [**Stoll v. King, 8 How 298 (NY 1953)**]

This should not be read to suggest that the ***p****rincipal* was justified in looking only to the confidence that he had in a trusted ***a****gent*. It did require conduct by the ***a****gent* which would result in the return of his funds. The purpose of using this case is to demonstrate that the underlying principle of *fiduciary* is that it contemplates ideas of *good faith* as the basis of transaction. It can be analogized to the relationship between the concepts of *oath* and *covenant*. The covenant of an individual is a promise that a certain act will be performed in consideration of the act of another person. In contrast, an oath is not predicated upon consideration, but is predicted on the integrity of the individual. Similarly, when an individual is placed in a particular position of serious trust which has as its underpinning the special relationship between the parties, the primary basis of the imposition of the obligation is based on integrity and not on legal obligation per se.

In contractual situations, the courts have consistently and historically sought to determine whether the required bargain existed to bring about a contract as well as fulfillment of the legal obligation of consideration. These determinations would appear to fall clearly into the parameters of the law courts. In contrast, the concept of *fiduciary* falls more into the historical category of equity courts wherein the underlying concepts are "fair play" and integrity. Fiduciary responsibility does not require the exactitude demanded under strict legal analysis. It is much more amorphous in nature and, hence, is more appropriately analyzed through an examination of the motives and actions of, and results achieved by the participants. But that examination is always accomplished in hindsight.

This position has been particularly well stated in a Michigan decision wherein the court stated, "Fiduciary relationship is one founded on

trust or confidence reposed by one person in the integrity and fidelity of another, and the term is a very broad one embracing both technical *fiduciary* relations and those informed relations which exist whenever one man trusts in and relies upon another." [**LaForest v. Black, 373 Mich 86, 128 NW2d 535 (1964)**]

Similarly, in Kentucky, the court held that a:

> [*F*]*iduciary* relationship exists when parties are under a duty to act for or give advice for benefit of another upon matters within the scope of a trust relation and where special confidence is reposed in another who in equity and good conscience is bound to act in good faith and with due regard to interests of one reposing confidence. [**Lappas v. Barker, 375 SW2d 248 (Ky 1963)**]

Another New York court said the term "requires that neither party exert influence or pressure upon the other or take selfish advantage of trust in such a way as to benefit himself or prejudice the other." [**Richardson Greenshields Secs, Inc v. Mui-Hin Lau, 693 F Supp 1445 (SDNY 1988)**]

A court in Missouri has gone so far as to suggest that it is the "reposing of confidence" that sets apart situations where the courts will impose a legal obligation of *fiduciary*. The court stated that:

> the Terms "Confidential" and "*Fiduciary*" are, in general application, synonymous; a confidential relationship exists between two persons, whether their relationships be such as are technically *fiduciary* or merely informal, whenever one trusts and relies on the other; the question in such case is always whether or not trust is reposed. [**Hodges v. Hodges, 692 SW2d 361, 377 (Mo Ct App 1985)**]

There is frequent use of the word reposed. Conceptually, *reposed* simply refers to something coming to rest. In this context it would appear to indicate a situation where the confidence of one individual has completely come to rest in another and the person reposing the confidence has no reason or desire to go elsewhere.

In a similar analysis, the Illinois court in **Schweickhardt v. Chessen, 161 NE 118 (Ill 1928)**, stated, "Where confidence is reposed by one party and accepted by the other, whether its origin is moral, social, domestic, or merely personal, the relation is *fiduciary*, and equity will regard the party's dealings according to rules applying to such relations."

In the specific arena of estate planning, an Illinois court observed, "As respecting undue influence in the making of wills, '*fiduciary* relationship' may exist as a matter of law between attorney-client, guardian-ward, trustee-beneficiary, and the like, or it may be the result of a more informal relationship-moral, social, domestic, or even personal in its origin." [***In re* Estate of Osborne, 128 Ill App 3d 453, 470 NE2d 1114 (1984)**]

An additional element in a *fiduciary* relationship has been suggested by a Texas court. The court stated:

> To establish a "*fiduciary relationship*," which generally arises over a long period of time when parties have worked together towards a mutual goal, for example, joint ventures, partners, attorney-client, and close family relationships, and may also arise where moral, social, domestic, or purely personal relationships of confidentiality, trust, and reliance are present, the evidence must conclusively show that dealings between the parties have continued for such a period of time that one party is justified in relying on the other to act in his best interest. [**Gonzales v. City of Mission, 620 SW2d 918 (Tex Civ App 1981)**]

Imposition of a *fiduciary* relationship is primarily determined in highly regulated matters by the statutes themselves governing a particular area of law. Employee Retirement Income Security Act (ERISA) seems to be one of those areas where the existence of a *fiduciary* relationship is strictly controlled by provisions of the statute.

In **Useden v. Acker, 721 F Supp 1233 (SD Fla 1989)**, the federal court in Florida held that a "[L]aw firm and attorney that drafted legal documents for a profit sharing plan, interpreted laws, and rendered legal advice to the plan were not '*fiduciary*' of plan."

Similarly, in a Minnesota case, the federal court stated:

> [E]ven if the attorney gave investment advice as to two investments made by Employee Retirement Income Security Act plans, rendering of such advice did not cause the attorney to become "*fiduciary*" within the meaning of the Employee Retirement Income Security Act, where the attorney had no discretionary authority or control with respect to purchasing or selling securities, and did not render investment advice on a regular basis. [**Anoka Orthopaedic Assoc, PA v. Mutschler, 709 F Supp 1475 (D Minn 1989)**]

However, where the attorney became involved with the actual management of pension plan assets, the court in **Bouton v. Thompson, 764 F Supp 20 (D Conn 1991)** held, the "[a]ttorney who renders professional services to an employer and its president may be "*fiduciary*" as defined by ERISA if the attorney exercises discretionary authority with respect to management of pension plan assets." [e.g.; a typical "**P**-**A**-**T**" arrangement.]

A Utah court has introduced what initially may seem an unusual characteristic of the *fiduciary* relationship and yet, as one considers the

reality of how people function when they rely on others with a near total confidence, it perhaps is a very astute observation. In **First Security Bank, NA v. Banberry Development Corp, 786 P2d 1326 (Utah 1990)** the court stated:

> Fiduciary relationship imparts a position of peculiar confidence placed by one individual to another; a "*fiduciary*" is a person with a duty to act primarily for the benefit of another and is in a position to have and exercise and does have and exercise influence over another; *fiduciary* relationship implies a condition of superiority of one of the parties over the other.

It is suggested that the idea of superiority of one party over the other is simply a recognition that when one acts without the scrutiny of the other by virtue of the trust relationship, it may well be appropriate to suggest that the party acting under the umbrella of the *fiduciary* relationship is, in fact, in a superior position.

In describing the general imposition of *fiduciary responsibility* on attorneys, it does not appear that the courts are prone to take into consideration the experience level of any particular attorney. The case law seems to suggest that if one has entered into the practice of law in a particular subject area, it is to be presumed that one has undertaken to provide services in areas in which one has adequate preparation. Whether this imposition rises to a level of creating an unrebuttable presumption is not clear. However, counsel may be well advised to consider the probability that in any given case, the court may hold that the experience level is irrelevant. The attorney who undertakes to provide a particular service will he held to a standard of care of a competent attorney in that particular field of endeavor.

Similarly, a Kansas court has held, "The term *fiduciary* connotes the idea of trust or confidence, contemplates good faith rather than legal

obligation as the basis of the transaction, refers to integrity and fidelity of the party trusted, rather than his credit or ability." [**Brown v. Foulks, 232 Kan 424, 657 P2d 501 (1983)**]

An Illinois court has defined the relationship between attorney and client (i.e.; "**P**-**A**") in the following terms. "An attorney and client relationship is '*fiduciary*' and the conduct of the attorney in his dealings with his client cannot be measured by the experience, or lack thereof, which the client has enjoyed." [*Ex parte* **Goodman, 377 Ill 578, 37 NE2d 345 (1941)**]

Section 1.03 Application to Wills and Trusts

In analyzing the obligations of *fiduciary responsibility* of the legal representatives of estate, legal counsel, and personal *agents* in the context of wills and trusts, there must first be an examination of at what point in the estate planning the analysis is being made.

By way of example, at the time that the initial meetings with clients and drafting are being undertaken, it would be difficult to perceive, in a normal relationship between attorney and clients, that there is at that point in time an affirmative obligation to beneficiaries. The only exception to this is the imposition of duty on the attorney to function on a professional level as set forth in the nationally precedent setting case of **Luau v. Hamm, 15 Cal Rptr 821 (1961)**.

In that case the court stated:

> The general rule with respect to the liability of an attorney for failure to properly perform his duties to his client is that the attorney, by accepting employment to give legal advice or to render other legal services, impliedly agrees to use such skill, prudence, and diligence as lawyers of ordinary skill and capacity

commonly possess and exercise in the performance of the tasks which they undertake.

However, in making that examination at any point in the estate planning process, it is appropriate for the *fiduciary* to keep in focus the five elements of negligence.

Sometimes in the hectic execution of estate planning, it is easy to forget fundamentals; therefore, if the professional will keep in mind the following elements, an analysis may become significantly easier.

The basic five elements in the common law for negligence are as follows:

1. Is there a duty of care to some individual(s)?

2. Has there been a breach of the duty?

3. Was the breach of the duty the proximate cause of the damage?

4. Were there any intervening causes?

5. Have there been actual damages?

The elements of a complaint for breach of *fiduciary responsibility* may include at least two additional elements that are not fundamental to the historical common law of the five elements of negligence. Thus, the seven elements that ought to be considered are as follows:

1. Is there a close personal relationship between the parties wherein reliance and confidence has reposed in the individual serving as trustee?

2. Is there a duty of care, confidence, and reliance?

3. Have assets been entrusted to the individual in whom the confidence has been reposed?

4. Has there been a breach of that duty?

5. Was the breach of the duty a proximate cause of the damage.

6. Were there any intervening causes?

7. Have there been actual damages?

These additional two elements are fundamental to the imposition of *fiduciary responsibility* which make it materially different from simple negligence. By pleading these additional elements, the higher level of responsibility imposed on the individual having *fiduciary responsibility* will be more carefully and clearly delineated.

If, when the prepared trust document is delivered to the *clients*, there are also accompanying pour-over wills signed and properly witnessed after the trust is signed, notarized, and initially funded; there is little likelihood that there could have been a breach of any duty of care against any party.

After a death of one of the spouses, the quality of the drafting and its implementation are going to become more likely to raise an issue of potential breach of duty.

If the trustee has failed to complete transfer of assets to the trust, a probate of assets may be needed which otherwise could have been administered under the trust arrangement if it had been fully funded.

It would be difficult to see that the trustee had breached any *fiduciary* obligation to a ***t**hird party* in situations where the trustor(s) and trustee(s) are one and the same individual(s). On the other hand, if the legal counsel, professional estate planner, or *fiduciary* failed to inform the trustors/trustees at the inception of the trust of the need to make transfers and to provide reasonable amounts of information, guidance, and assistance in making those transfers, then there may be an adjudication that there has been a failure to fulfill obligations to the then beneficiaries of the trust. [e.g.; another typical "**P**-**A**-**T**" arrangement.]

It seems improbable that there would be any basis for claiming that there is a breach as to any beneficiary who would only receive benefits of the trust after the death of both initial trustors-trustees.

Upon the death of both the trustors and trustees, however, there may now come to be expanded liability to subsequent beneficiaries. This position is clearly analyzed in **Lucas v. Hamm, 15 Cal Rptr 821 (1961)**, under a third-party beneficiary contract theory.

The distinction between liability to the beneficiaries in a situation where the representation was limited only to the original trustors/trustees as compared to continued representation of a new trustee is much more difficult.

Section 1.04 Detailed Elements of Fiduciary Responsibility for Trustee

In analyzing the elements found in the cases reported at **§1.03**, by reducing the key elements of those cases to questions one may ascertain whether a *fiduciary responsibility* exists and, more important, whether that responsibility has been fulfilled. What follows

is a series of questions which, it is hoped, will provide a thought process to assist in making those determinations.

What has been attempted is to review a large number of cases throughout the United States in an attempt to characterize those elements which appear to be consistently followed in the case law concerning *fiduciary responsibility*. In some cases, it became evident that some courts recognized that there were nearly unique characteristics which set apart a cause of action for breach of *fiduciary responsibility* as compared to the historical elements of a cause of action in negligence.

Section 1.05 Questions to Be Analyzed to Determine Presence of Fiduciary Responsibility

1. How long has there been a relationship of confidence between the parties?

2. Has there been a long period of association and working together between the parties?

3. Is there any social, domestic, or moral origin in the relationship between the parties?

4. Is there any family relationship with relevance to the transaction?

5. What have been the past relationships of the parties?

6. How many times have there been similar types of relationships between the parties?

7. Has the confidence of an individual been reposed in the trusted person?

8. Is the individual justified in reposing the confidence relevant to the transaction?

9. How significant is the level of reliance on the transaction?

10. Has the ***p****rincipal* chosen the trusted person by virtue of the confidence in him or her rather than the individual's ability?

11. Has the confidence of the creator of the trust or beneficiary reposed in the trustee?

12. Is there a peculiar level of confidence existing between the parties involved?

13. Has there been any unusual influence or pressure exerted by the trusted party?

14. What is the practical involvement of the trusted party in the transaction?

15. How complicated is the transaction?

16. Are there statutory impositions of *fiduciary* responsibility?

17. What is the experience of the trusted person in these matters?

18. What is the respective knowledge and authority of the parties as compared to that of the trusted person in the transaction?

19. How much control does the trusted person in functional terms have over the assets or the business interest?

20. Does the trusted person have functional control over the primary aspects of the transaction?

21. Is the trusted person acting on behalf of others without any personal conflict of interest?

22. Is there any question of the integrity or fidelity of the trusted person in his or her conduct?

23. Is there any question of unfair dealing?

24. Is there any issue concerning good faith?

25. Is the conduct in which the trusted person is engaged imprudent?

26. Is there an inherent conflict of interest under the facts of the situation?

27. Has the conduct of the trusted person resulted in his or her own benefit?

28. Has the conduct of the trusted person prejudiced the benefit others?

29. Under what circumstances could the conduct be justified?

30. Is this a situation where the trusted person should have sought outside assistance?

31. Does there appear to be a superiority in the position of the trusted person?

32. What is the quality of the drafting of the documents?

33. What research was undertaken to ensure compliance with the law?

34. Does there exist as a matter of law a *fiduciary* relationship?

35. Is there an *agency* relationship involved in the matter?

36. Was the *agency* relationship founded in reliance on the trusted person?

37. Has past conduct of the trusted person or attorney been such as to justify a continuing level of confidence and reliance?

Undoubtedly, there are many other questions which could be asked, but it is suggested that any time an attorney or trusted person is placed in a position where it must be determined whether there is a *fiduciary responsibility*, and whether there has been a fulfillment of that responsibility, the answer can only be given after answering a series of other questions suggested in this section.

Section 1.06 Ongoing Opportunity for Professional Advisors

Experience has demonstrated that providing a client with a checklist of events and circumstances which may suggest making changes to a trust may assist the family to more fully realize estate planning goals.

Where clients are given a checklist, it may be helpful to hold a personal meeting between the estate planner and client. That meeting will facilitate a thorough discussion of the methods and options suggested by the checklist.

For example, it is not unusual for clients to indicate they have serious problems with one of their children due to what they perceive as a questionable marriage. When clients find that they can protect a child from him or herself and a questionable spouse through the use of a life estate arrangement for the interest of that particular child, this is normally a source of significant personal relief.

One example may be particularly helpful. A serious dispute had arisen between an elderly couple concerning one daughter married to a man who was clearly on the fringes of society. Because of the mother's personal affection for the daughter, notwithstanding the son-in-law's ethics and moral standards, she was prepared to allow funds to be distributed to the daughter outright, instead of having them rigidly controlled. On the other hand, the husband wanted all assets to he strictly controlled, with distribution only of income and without discretion of distribution of principal.

When a personal discussion with the clients finally occurred, it was explained to them that it would be possible to have a co-trusteeship act as a monitor for invasion of principal. With that change, the husband was willing to relent from his very rigid position and allow for invasion of principal to maintain basic standard of living.

Similarly, when it was demonstrated that the provision could be drafted so that in the event of either the demise of the son-in-law or dissolution of the marriage, the daughter's share would be immediately distributable to her, the mother felt mollified and agreed that this was a reasonable way to balance the protection of her daughter and the desire to not withhold the family fortune from her.

Section 1.07 Does Future Advice Become Obligatory?

Given the unusual, continual changes in tax and estate planning law and inherent changes in all family relationships, the question arises of the *fiduciary responsibility* of the professional in keeping the client advised of material law changes. This is an area in which there is a deficiency of information concerning whether this rises to the level of *fiduciary responsibility*. It is our opinion that it does not.

However, in an abundance of caution, when the comprehensive change in federal tax law took place in 1981, in the desire to serve clients as well as to protect against any claim of malpractice, the Attorney held a full day seminar concerning the changes in the federal tax law.

All clients were invited who had been previously represented by the Attorney in the estate planning process. Detailed information was provided both in person and in writing. Tapes from the lectures themselves were provided for clients who desired to pay for them at cost.

Even though it is not clear whether this kind of project is obligatory in the fulfillment of *fiduciary responsibility* to the clients or whether it is simply an opportunity to appropriately serve clients, prudence dictates perceiving it as a legal obligation.

When there is a/are substantial change(s) in the law which will materially affect existing documents; one can certainly make a strong argument that the unknowing public who engages the services of the professional estate planner has the right to be appraised of the change(s), the explanation such change(s), and the implication(s) those changes might have in light of their estate planning. If the clients do have such a right, then there is a corollary duty of *fiduciary responsibility*.

In addition to situations where there has been a significant change in tax law or other substantive areas of the law affecting estate planning, as has been previously suggested, a checklist for determining circumstances which would suggest the amending of a trust may be helpful.

Each professional will want to expand the list under any of the headings to encompass those areas where he or she has found material changes that have caused a need to consider modification of existing estate planning documents.

The most important recognition involved in the process is that imposition of *agency* and *fiduciary responsibility* is not designed to be punitive in effect ... it is designed to facilitate and maximize success in quality estate administration.

Law and Purpose of Agency

Section 2.01 Law and Purpose of Agency

Agency is derived from the Latin verb, *agere*, meaning to act (*ago*, *agere*, *egi*, *actum*).

While the law of *agency* is *sui generis*, having developed such distinctive rules as ratification, undisclosed principal, vicarious tort liability, and other inherent *agency* power, many of its rules are derived from contracts, torts, restitution, and trusts, especially the *fiduciary* concepts of trust law.

The primary purpose of *agency* is to enable a person to accomplish results through the services of others, thereby enlarging the scope of such person's activities. One who acts through another is considered by the law of *agency* as acting oneself.

Most of the world's work is performed by ***a**gents*. The employees (i.e.; the ***p**rincipal*) of an individual proprietor are the latter's ***a**gents* (i.e.; ***t**hird parties*). In a partnership, each general partner is the general agent of the other partner or partners. This is known as mutual *agency* (i.e.; a complete "**P**-**A**-**T**" relationship). Employees of the partners also are ***a**gents* of the partners. The rights and liabilities of partners with respect to each other and to ***t**hird parties* are largely determined by *agency* ***p**rinciples*. Between the members of a joint venture, there is also a mutual *agency*. In a joint stock association, the officers and other employees are ***a**gents* of some or all of the members. In the business corporation they are, under the corporate entity concept,

***a**gents* of the corporation. The contractual relationships that exist within unincorporated common law business enterprises (i.e., business trusts, land trust, pure equity trusts, contractual companies, etc.) also create *agency* between the beneficial holders and the administrators, executors, guardians, receivers, trustees, and any employees of the unincorporated entity.

Section 2.02 Definitions and Creation of Agency

Terminology in the cases and commentaries is not consistent, especially prior to the "Restatement of Agency", first published in 1933, and re-restated in 1958. Yet liability often depends upon classification of the persons involved. These and other concepts frequently determine liability. Definitional precision promotes understanding and communication, but does not necessarily assure predictability. Basic policy choices are reflected in the principles of *agency* law. The application of such principles by the courts can involve linguistic ingenuity.

The three-volume "Restatement (Second) of Agency" (1958) contains the following definitions:

> *Agency*: "the *fiduciary* relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act..."
>
> *Principal*: "the one for whom action is to be taken..."
>
> *Agent*: "the one who is to act..."
>
> *Master*: "a ***p**rincipal* who employs an ***a**gent* to perform service in his affairs and who controls or has the right to control the

physical conduct of the other in the performance of the service..."

Servant: "an ***agent*** employed by a master to perform service in his affairs whose physical conduct in the performance of the service is controlled or is subject to the right to control by the master..."

Independent Contractor: "a person who contracts with another to do something for him but who is not controlled by the other nor subject to the other's right to control with respect to his physical conduct in the performance of the undertaking. He may or may not be an ***agent***..."

Employer: "the one for whom action is to be taken..."

Escrow: "An escrow is a deed, money or chattel delivered to a person, the holder, by another and which the holder contracts to retain until the happening or non-happening of an event; if the event happens, or fails to happen, before a specified time, the escrow is to be delivered to a ***third person***; otherwise he is to return it to the depositor..."

Subagent: "A person appointed by an ***agent*** empowered to do so, to perform functions undertaken by the ***agent*** for the ***principal***, but for whose conduct the ***agent*** agrees with the ***principal*** to be primarily responsible..."

Universal Agent: "an ***agent*** authorized to conduct every transaction lawfully delegable by the ***principal*** to the ***agent***..."

General Agent: "an ***agent*** authorized to conduct a series of transactions involving continuity of service..."

Special Agent: "an ***agent*** authorized to conduct a single transaction or a series of transactions not involving continuity of service..."

Power: "an ability on the part of a person to produce a change in a given legal relation by doing or not doing a given act..."

Authority: "the power of the ***agent*** to affect the legal relations of the ***principal*** by acts done in accordance with the ***principal***'s manifestations of consent to him..."

An *agency* is a consensual relationship which is created and exists only when one person manifests an intention that another shall act for such person and the other consents so to represent such person. The relationship being not necessarily contractual or *fiduciary*, consideration is not necessary to the creation of the *agency* and contractual capacity of both parties is not required.

Ordinarily, no formality is required for the creation of an *agency*. It may be created orally or in writing, or by some other conduct by the ***principal*** which indicates an intention to appoint an ***agent***.

While an *agency* can be formed orally, the Statute of Frauds might require a writing: (1) Grants of certain interests in real property might have to be in writing signed by the grantors or "their agents thereunder lawfully authorized by writing"; (2) Agreements of guaranty; (3) Agreements not to be performed within one year might have to be in writing signed by the party to be charged or "some other person thereunder by him lawfully authorized"; and (4) Contracts for the sale of personal property above a certain price might have to be in writing signed by the parties to be charged by such contract or "their agents thereunder lawfully authorized".

Conclusion

This text was designed to address three kinds of activities: *First*, the preparation of proper documentation; *Second*, the methods by which the advisor manages the flow of work activities with the client and within the office; and, *Third*, instructions and documentation to be provided to clients to ensure that they are able to properly fulfill their *fiduciary responsibility*.

These topics are not always presented in that exact sequence. At each stage, there may be elements of each of them involved.

Nonetheless, the emphasis of the text is on mechanical procedures and not on substantive law.

In the completion of all the various tasks addressed, it should always be kept in mind that the umbrella over all activities concerning the utilization of trusts and estate planning and the mechanical procedures is *fiduciary responsibility*.

As previously suggested, *fiduciary responsibility* is not only the roof of the "house of the quality estate planning," it is also the walls that maintain the integrity of the entire structure. If the professional is able to maintain an internal, instinctive understanding of *fiduciary responsibility*, *agency law*, and carry the sometimes onerous obligation imposed on trustees and executors, then the entire estate planning procedure will be greatly facilitated.

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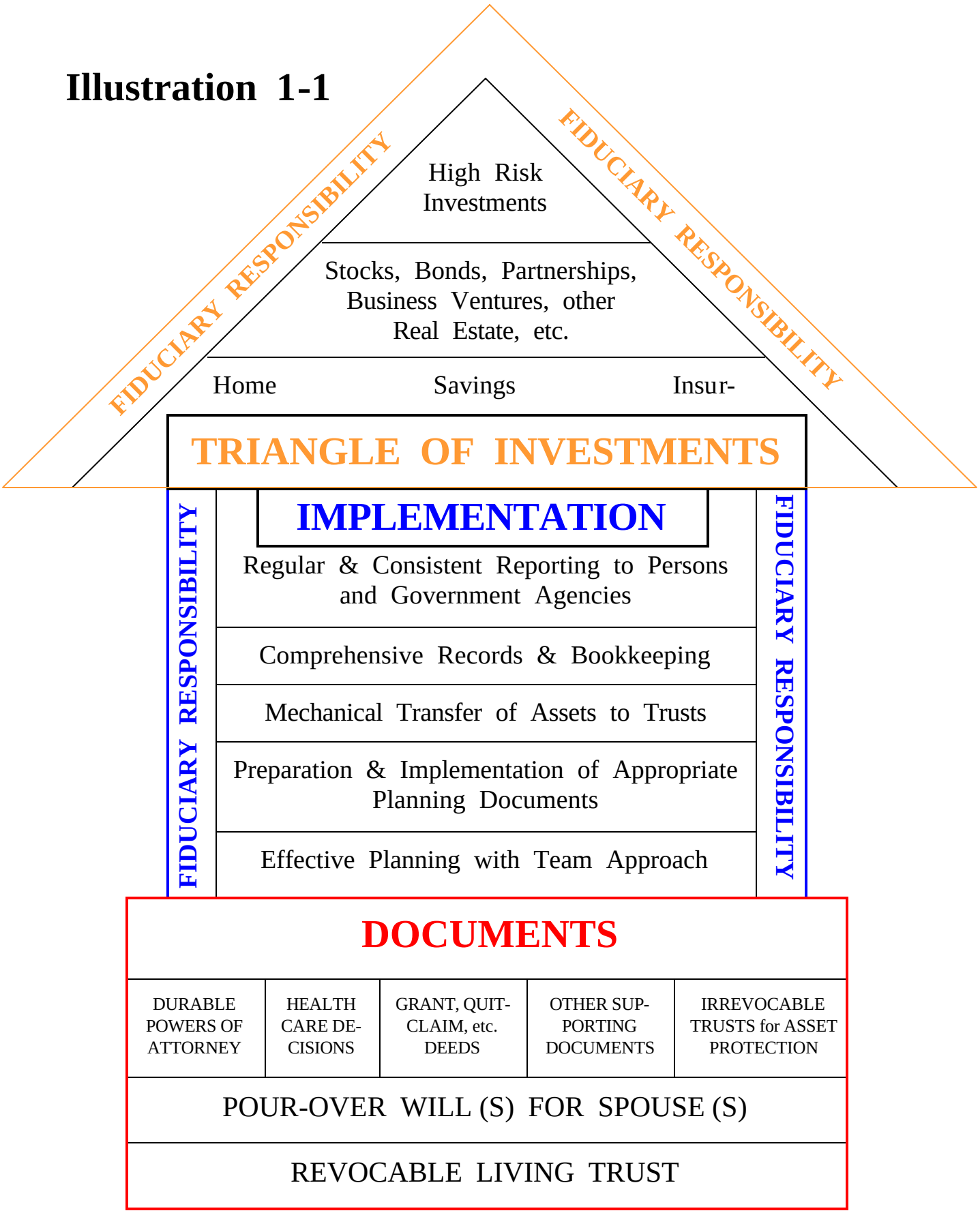
Illustration 1-1



HOUSE OF FIDUCIARY RESPONSIBILITY

Types of Trust Chart

The following chart is only a partial list of all the types of trusts available. There are a host of other "so-called" trusts with expensive names and fancy lables but when reduced to their basic objectives; fit into one of the categories listed below. In either event; every entity below requires the highest degree of fiduciary responsibility over not only the conservation of the assets but the distribution of assets, income, interest, dividends, etc. Taxes need to be paid, investments must be wisely considered, and books still have to be kept. Please consider the best person, individual or corporate, for the task set before them. Select the most competent, not necessarily the first born to fill those shoes.

Type / Name(s) of Trust:	Brief description of what it does:
1041	A contractual business entity cast in the form of a trust. Used "in conjunction with" or "in place of" sole proprietorships, corporations, partnerships, joint ventures, etc.
2503(c)	Protects minor children while still qualifying for maximum gift tax benefits.
$5000 or 5%	Allows a beneficiary to demand a non-accumative distribution of $5000 or 5% of the trust assets each year in addition to any others rights to income, interst, dividens, etc
Alimony	Utilized to pay alimony to your ex-spouse insuring that the ex-spouse pays all income taxes that arise from the trust; not the creator of the trust.
Asset Protection (APT)	Usually a forgein trust created to protect assets. Also see 1041.
Charitable Lead Annunity	This is a charitable lead trust where the payment is based on an annunity.
Charitable Lead (CLT)	You give $$$ or property to the trust, the charity(ies)receive annunity payments, and your designated beneficiary(ies) get all the principal when the trust ends.
Charitable Lead Unitrust	This is a charitable lead trust where the payment is based on a unitrust payment.
Charitable Q-TIP	A trust for the spouse's benefit which upon their death is paid to a charity.
Charitable Remainder Annunity (CRAT)	A charitable remainder trust that makes payments to you based on annunity payments (a fixed percentage of the initial value of the funding assets).

Charitable Remainder (CRT)	This trust is funded with unencumbered but highly appreciated assets such as real estate, stocks, etc. The trustee sells the assets devoid of capital gains taxes. You & your spouse receive annual income and upon death of the principal(s); the charity receives the remainder of the principal, if any exists. Meanwhile, you get the charitable tax contribution based on the present value of the chatiy's future interest.
Charitable Remainder Unitrust (CRUT)	This is a charitable remainder trust that makes payments to you based on a fixed percentage of the assets (usually easily valued) owned by the trust each year.
Children's	Sometimes called a Minor's Trust ...is for children, grandchildren, or other minors is designed to qualify for the $10,000 annual exclusion.
Christofoni	This provision is usually coupled with a Crummey trust to allow the same annual exclusions be afforded even to a grantors' grandchildren.
Complex	Is allowed to accumulate income and not distribute it annually. See Simple.
Credit Shelter (CST)	This trust is more commonly referred to as the "A" trust; Bypass Trust; Unified Credit Trust, etc. is used to double thew lifetime exclusion for married couples.
Crummey	This trust contains unique provisions that allow you to make completed gifts for your children that qualify for the annual exclusion amount that can be taken or refused.
Foreign Situs	A trust formed in a foreign county for legal or tax benefits.
Generation Skipping Transfer (GST)	Used to transfer the $1 million GST tax exemption to the grantor's grandchildren. It minimized the impact of extremely costly generation skipping tax transfers.
Grandchildren's	Grandparents establish this trust to provide for the education of their grandchildren.
Grantor Retained Annunity (GRAT)	A gift made now, for which the grantor keeps receiving the income each year based on annunity payments, for any nunber of years the grantor desires.
Grantor Retained Interest (GRIT)	In this arrangement, the grantor retains an interest (e.g., the right to all income) for a specified period of time. The principal is then given to the beneficiaries.
Grantor Retained Unitrust (GRUT)	For a gift made now, the grantor keeps getting annual income based on the fair market value of the property, for a specified period of time.
Irrevocable Life Insurance (ILIT)	This trust is used to keep large insurance policy proceeds out of your estate. It also protects valuable insurance proceeds from creditors.
Inter Vivos (Living)	This is the stock, standard, "A", "A-B", or "A-B-C" family trust setup.
Inter Vivos Credit Shelter	Allows you to use pension or IRA assets to fund a credit shelter trust to utilize your unified credit amount.

Inter Vivos Q-TIP	Permits you to fund a Q-TIP (marital) trust with pensions or IRAs.
Irrevocable	A trust that cannot be altered, ammended, or changed by the creator.
Massachusetts Realty	A real estate holding trust unique to the State of Massachusetts.
Medicaid Avoidance	Keeps your, or your special child's, assets safe from nursing home/Medicaid claims.
Multiple Children's	Sets up separate trust for each child. Keeps their assets safe from creditors.
Personal Residence (PRT)	Used to remove your primary/vacation home from your estate at a reduced tax rate.
Pooled Income	You can contribute property and in exchange participate in the investment pool managed by the charity for the term of the trust.
Pot	This is a single trust set up for all your children beneficiaries to be distributed based on the need of each child.
Qualified Domestic (Q-DOT)	Obtains maximum gift or estate tax savings by qualifying a gift or bequest to your spouse who is not a US citizen.
Qualified Personal Residence (QPRT)	A trust used to remove the value of your primary/vacation home from your estate at a discounted gift tax rate.
Qualified Subchapter S (QSST)	A special trust utilized to hold "S" corporation stock without jeo[ardizing "S" corporation tax benefits.
Qualified Terminal Interst Property (Q-TIP)	Commonly referred to as the "C" trust; it has many uses (e.g., excesses above the first to die grantor's lifetime exeption is placed inside it for federal tax deferment).
Rabbi	This trust is used to provide a degree of asset protection for compensation benefits.
Revocable	Just the opposite of an irrevocable trust.
Right of Election	Allows a spouse the least amount of assets allowed by law with the most control over where those assets will be distributed upon death.
Special Needs	Gives protection to the assets and provides for a child/beneficary with special needs.
Spendthrift	A simple provision that prohibits assets from a beneficiary's creditors.
Sprinkling	Used with flexibility for the trustee to distribute income and assets to beneficiaries.
Unitrust	A type of grantor retained or charitable remainder trust.
Voting	Provides control of stock in closely held or family businesses to assure management and operations as you determine best.
Zero Inclusion	A trust for grandchildren which are planned for for GST exemption.

Selecting the Trustee of a Trust without violating the Grantor Trust Rules

This lists those powers a grantor, or his or her spouse, a non-adverse party, an independent party, or an adverse party, may hold as trustee without causing the grantor to be taxed as the trust's owner under Section 671.

Grantor or anyone else may hold these powers:

9 Manage the trust assets, including:

- **Ž** Selecting trust investments, unless the trust owns closely held stock, and its interest plus that of the grantor are significant with respect to control.
- **Ž** Voting stock owned by the trust, unless the trust owns closely held stock and its interest plus that of the grantor are significant with respect to control. (***IRC § 675(4)***)

9 Make mandatory distributions of income or principal, except that the grantor is still taxed on any payments that discharge his or her legal support obligations. (***IRC § 674(b)***)

9 Appoint or otherwise control the trust's beneficial enjoyment under a power exercisable solely by will, unless the grantor also can accumulate trust income for disposition at his or her death. (***IRC § 674(b)(3)***)

9 Allocate trust income or principal among charities. (***IRC § 674(b)(4)***)

9 Distribute principal among income beneficiaries under a reasonably definite standard, unless someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(b)(5)(A)***)

9 Distribute principal to an income beneficiary, charging it against his or her separate share of principal, unless someone can add beneficiaries, other than adding after-born or after-adopted children. (***IRC § 674(b)(5)(B)***)

9 Withhold income if it must ultimately be payable to:

- **Ž** The beneficiary, or
- **Ž** The beneficiary's estate, or
- **Ž** The persons named under the beneficiary's broad limited power of appointment, or
- **Ž** The income beneficiaries when the trust terminates in stated shares.

9 Withhold income, unless someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(b)(6)***)

9 Withhold income temporally during the beneficiary's disability (including minority). (***IRC § 674(b)(7)***)

9 Allocate receipts and disbursements between principal and income, even if expressed broadly. (***IRC § 674(b)(8)***)

9 Retain reversionary interest with a value, on the trust's creation or the funding of the particular share, worth not more than five (05%) percent of the whole trust fund. (***IRC § 673***)

9 Lend trust funds to anyone without adequate interest and security. (***IRC § 675(2)***)

9 Borrow trust funds with adequate interest and security, if repaid before the taxable year. (***IRC § 675(3)***)

9 Control or alter the trust's beneficial enjoyment, but only after a period that, were it a reversionary interest, would satisfy the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 674(b)(1)***)

9 Revoke the trust after a period that, were it reversionary interest, would be permissible because the interest would satisfy the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 676(b)***)

9 Be a possible income beneficiary (current or accumulated) after a period that, were it a reversionary interest, would satisfy the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 677(b)***)

9 Have the possibility that the trustee will use trust income to pay the premiums on life insurance policies on the grantor's or his or her spouse's life, after a period that, were it a reversionary interest, would satisfy the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 677(b)***)

Any nonadverse party, as trustee, may hold these powers:

9 Do all the things the grantor could do.

9 Allocate income among beneficiaries under a reasonably definite external standard in the trust instrument, unless:

- **Ž** The trustee is the grantor's spouse,
- **Ž** Someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(d)***)

An independent trustee may hold these powers:

9 Do all the things the grantor could do.

9 Do all the things a nonadverse trustee could do.

9 Lend trust funds to the grantor without adequate interest and security, if:

- **Ž** He or she is empowered to lend to the general public, and
- **Ž** The loans are repaid before the taxable year. (***IRC § 675(2)***, *(3)*)

9 Allocate income and/or principal among beneficiaries without a definite standard, unless someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(c)***)

An adverse party may hold these powers:

9 Do all the things the grantor could do.

9 Do all the things a nonadverse trustee could do.

9 Do all the things an independent trustee could do.

9 Revoke the trust and revest the trust funds in the grantor. (***IRC § 676(a)***)

9 Pay trust income to or accumulate it for the grantor or the grantor's spouse. (***IRC § 677(a)***)

9 Use trust income to pay premiums on a policy of insurance on the life of the grantor or the grantor's spouse. (***IRC § 677(a)***)

Selecting the Trustee of a Trust without violating the Grantor Trust Rules or Causing Estate Taxation

This lists those powers a grantor, a non-adverse party, an independent party, or an adverse party, may hold as trustee without causing the grantor to be taxed as the trust's owner for either income or estate tax purposes.

Grantor or anyone else may hold these powers:

9 Manage the trust assets, including:

- Selecting trust investments, unless the trust owns closely held stock, and its interest plus that of the grantor are significant with respect to control.
- Voting stock owned by the trust, unless the trust owns closely held stock and its interest plus that of the grantor are significant with respect to control. (***IRC §§ 674(b)(8) & 675***)

9 Make mandatory distributions of income or principal, but the grantor should be precluded from using trust funds to discharge his or her legal support obligations, since such actual income payments are taxed to the grantor (***IRC § 677(b)***) and the right to make them is a general power of appointment, causing the trust funds to be included in his or her gross estate (*Reg § 20.2036-1(b)(2)*).

9 Distribute principal among income beneficiaries under a reasonably definite standard, unless someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(b)(5)(A)***; ***Budlong v. Commissioner, 7 TC 756 (1946)***)

9 Lend trust funds to the general public without adequate interest and security. (***IRC § 675(2)***)

9 Borrow trust funds with adequate interest and security, if repaid before the taxable year. (***IRC § 675(3)***)

Any nonadverse party, as trustee, may hold these powers:

9 Do all the things the grantor could do.

9 Control the trust's beneficial enjoyment, but only after a period that, were it a reversionary interest, would satisfy the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 674(b)(2)***)

9 Appoint or otherwise control the trust's beneficial enjoyment under a power exercisable solely by will, unless the nonadverse party also can accumulate trust income for disposition at his or her death. (***IRC § 674(b)(3), 2041***)

9 Allocate trust income or principal among charities. (***IRC § 674(b)(4)***)

9 Distribute principal to an income beneficiary, charging it against his or her separate share of principal, but a grantor trust is created if someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(b)(5)***; ***Estate of Varian v. Commissioner, 47 TC 23 (1966)***)

9 Withhold income if it must ultimately be payable to:

- Beneficiary, or
- Beneficiary's estate, or
- Persons named under the beneficiary's broad limited power of appointment, or
- Income beneficiaries when the trust terminates, in stated shares.

This creates a grantor trust if someone can add beneficiary's disability (including minority). (***IRC § 674(b)(6)***; ***United States v. O'Malley, 383 US 627 (1966)***)

9 Withhold income temporally during the beneficiary's disability (including minority). (***IRC § 674(b)(6)***)

9 Allocate receipts and disbursements between principal and income, even if expressed broadly. (***IRC § 674(b)(4)***)

9 Revoke the trust after a period that, were it the grantor's reversionary interest, would have satisfied the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 676(b)***)

9 Pay trust income to or accumulate it for the grantor or the grantor's spouse, after a period that, were it the grantor's reversionary interest, would have satisfied the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 677(b)***)

9 Use trust income to pay premiums on a policy of insurance on the life of the grantor or the grantor's spouse, after a period that, were it the grantor's reversionary interest, would have satisfied the rules of Section 673 (but the trust becomes a grantor trust when the power vests). (***IRC § 677(b)***)

9 Allocate income among beneficiaries under a reasonably definite external standard in the trust instrument, if the trustee is not the grantor's spouse, unless someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(d)***)

An independent trustee may hold these powers:

(*See* ***Revenue Ruling 79-353, 1979-2 CB 325****, in which the IRS said that a grantor who could, without restriction, remove one independent trustee and replace it with another was treated as holding the trustee's powers directly.*)

9 Do all the things the grantor could do.

9 Do all the things a nonadverse trustee could do.

9 Lend trust funds to the grantor without adequate interest and security, if:

- **Ž** The trustee is empowered to lend to the general public, and
- **Ž** The loans are repaid before the taxable year. (***IRC § 675(2)***)

9 Allocate income and principal among beneficiaries without a definite standard, unless someone can add beneficiaries, other than after-born or after-adopted children. (***IRC § 674(c)***)

An adverse party, as trustee, trustee may hold these powers:

9 Do all the things the grantor could do.

9 Do all the things a nonadverse trustee could do.

9 Do all the things an independent trustee could do.

9 Revoke the trust and revest the trust funds in the grantor. (***IRC § 676(a)***)

9 Pay trust income to or accumulate it for the grantor or the grantor's spouse. (***IRC § 677(a)(2)***; *Estate of Wells v. Commissioner*, *¶ 83,574 P-H Memo. TC (1983)*; ***Outwin v. Commissioner, 76 TC 153 (1981), acq. 1981-1 CB 2***.)

9 Use trust income to pay premiums on a policy of insurance on the life of the grantor or the grantor's spouse. (***IRC § 677(a)(3)***)

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