Pro or No? Picking a Trustee

By Anna Prior

When setting up a trust, people often turn to a relative or confidant to oversee it.

That is natural enough, considering trusts frequently have a highly personal purpose—passing on wealth to loved ones—in addition to a common aim of minimizing taxes. Who better to serve as trustee than someone who has been part of your life for many years?

But ties of friendship and family can be complicated by emotions and other factors. And a close relationship isn't necessarily the best qualification for grasping and carrying out the terms of a trust, estate planners say. In many situations, designating a professional trustee may be a better option, even if it comes with its own issues, such as higher costs.

The use of nonprofessional trustees appears to be growing as more people are setting up trusts to function in their own lifetimes, says Adrienne Penta, who oversees the trust operations and wealth-planning services in Boston for Brown Brothers Harriman Private Bank, which manages $26.5 billion.

"They feel like they don't need a professional because they can keep an eye on it while alive," she says.

Estate-Tax Thresholds

Trusts typically make the most sense for people planning to leave more than $5 million—or $10 million for a couple—now that the threshold for paying federal estate taxes was set at those levels two years ago and indexed to inflation. (For 2015, the exemption levels are $5.43 million and $10.86 million, respectively.)

Still, other people might want a trust to minimize state estate taxes or exert greater control over their financial legacy.

For example, parents passing along a large estate to their children may want to put conditions—such as finishing college or encouraging charitable donations—on how and when those assets are distributed after the parents die.

A pro trained in the ins and outs of trusts can be especially helpful for handling complicated, long-term "dynasty trusts"—those designed to last for multiple generations, says Jonathan Forster, a tax and estate lawyer at the McLean, Va., office of law firm Greenberg Traurig.

"You'll almost have to hire a professional trustee, because no individual that you pick will last long enough to do the job," he says.

A pro also is likely to be more removed from family or personal dramas. "When you put someone between a beneficiary and their money, you're pressing for some problems," Mr. Forster says. "The perception with a professional or an institution is that they are acting independently, rather than it looking like Uncle Joe doesn't want you to live in a house more expensive than his."

Ms. Penta says her firm recently discovered a trust that had terminated many years ago. The assets should have been distributed outright to the beneficiary, but the trustee—a business acquaintance of the trust's creator—wasn't paying attention and didn't realize that the trust had terminated.

This created a number of legal issues, she says, because the assets were no longer owned by the trust and had to be retitled in the name of the beneficiary before any further investment decisions could be made.

There can be downsides to choosing a pro over a family member or friend. Professional trustees, such as trust companies, often charge a fee based on the assets in the trust, Ms. Penta says. She says it isn't unusual for a pro to charge an annual fee of 0.20% or 0.25%, or $20,000 or $25,000 for a $10 million trust.

There may also be concerns that a pro—despite a fiduciary obligation to always act in the trust beneficiary's best interest—may nonetheless be more focused on the bank's interests than the needs of the family.

"A nonprofessional is always going to have the soft side, they are going to know the people, understand their problems, understand their idiosyncrasies," Mr. Forster says.

In the case of a trust that oversees a family business or property, an associate who has long been familiar with that asset and how it functions may have an advantage, he says.

In some estate plans, co-trustees are designated, one of them a pro and the other a family member or other nonprofessional. Such compromise arrangements can vary, with some requiring co-trustees to agree on all decisions and others dividing up responsibilities.

For instance, a trust company can track tax issues, issue account statements and make investment decisions, and the nonprofessional trustee can be in charge of making decisions about distributions, Mr. Forster says.

Replacing a Trustee

Experts say individuals setting up trusts should make sure their trust documents include a mechanism for removing and replacing a trustee, regardless of whether it is a pro or your uncle.

"These agreements can be in existence for decades and decades, and circumstances can change over time, so these documents need to be drafted so there can be some flexibility," says Rebecca Milliman, a Chicago-based managing director for Atlantic Trust Private Wealth Management, which oversees $25.9 billion.

One tactic, she says, is to name a so-called trust protector, who can make various administrative changes to the trust document, including the removal of a trustee, without needing to take the matter to court.

Some trusts even give a beneficiary the power to remove and appoint successor trustees. "Having some of those discussions when it isn't working out can be uncomfortable or awkward, especially with a family member," Ms. Milliman says. "But it's important that the beneficiary go to the trustee, respectfully thank them for their service, but say we're going to make a change."