



Overview

A trust protector is an individual, group of individuals, or entity with specified powers over a trust. A trust protector's powers may be extremely narrow in scope, limiting the protector to an exclusive list of actions, such as the ability to remove and replace the trustee or to make discretionary distributions of trust assets. Alternatively, a trust protector may be given broad powers, such as to modify terms of the trust, terminate the trust, or add or remove trust beneficiaries.

In addition, a trust may provide that the position of trust protector only comes into existence upon certain triggering events. A grantor may find it appropriate to name a trust protector to provide additional flexibility to an irrevocable trust to ensure that the grantor's original intent is carried out. A trust protector may hold powers which, if held by the trust grantor, would result in estate inclusion..

Description

A trust protector may be given the following authority to:

- ◆ Change trust situs or governing law;
- ◆ Remove, add and/or replace trustees;
- ◆ Appoint a successor trust protector;
- ◆ Amend the trust with regard to administrative or dispositive provisions;
- ◆ Amend or modify the trust provisions to respond to changing tax and state law;
- ◆ Make tax elections (ex: QTIP, S Corp qualification, etc.);
- ◆ Appoint agents to carry out responsibilities under the trust agreement;
- ◆ Veto or direct trust distributions;
- ◆ Alter distributions among beneficiaries;
- ◆ Add or remove beneficiaries;
- ◆ Consent to the exercise of a power of appointment;
- ◆ Modify or grant a power of appointment;
- ◆ Direct, advise, veto, and/or consent to trust investments;
- ◆ Consent to allow trustee self-dealing;
- ◆ Change the trust situs;
- ◆ Interpret terms of the trust in the event of ambiguity;
- ◆ Expand or limit the powers of the trustee; and/or
- ◆ Modify, merge, or terminate the trust.

Who should be chosen to serve as a trust protector?

The role of trust protector should be filled by an individual or entity familiar with the grantor's intent, as well as the circumstances surrounding the trust beneficiaries. Special care should be taken to ensure that there is no implied agreement between the grantor and the protector such that it could be concluded that the grantor is actually directing the actions of the trust. The trust protector should be a person or entity other than the trust grantor, the grantor's spouse, a trust beneficiary, or a person with a legal obligation with respect to a beneficiary to avoid adverse tax consequences. An insured on a policy held by the trust should generally not be named as trust protector.

Tax Implications

Granting certain powers to a trust protector can lead to adverse or unanticipated tax consequences.

Estate Tax

Powers exercisable for the benefit of the protector can cause inclusion of trust property in the protector's estate as the power would likely be considered a general power of appointment over trust assets. If the protector is able to exercise a power in favor of someone to whom the protector owes a legal obligation for support, such power could also result in assets being included in the protector's estate.

Any type of prearrangement between the grantor and the trust protector that the grantor will informally retain any form of control or influence over trust assets should be strictly avoided as this type of understanding could cause estate inclusion in the grantor's estate.

Income Tax

Certain powers to add a trust beneficiary, alter distributions or amend the trust may cause the trust to be considered a grantor trust as to the protector for income tax purposes.

Gift Tax

Giving a trust protector the ability to modify trust provisions should be done with caution. For example, if the protector is given the power to amend withdrawal rights, such modifications should not impair a Crummey withdrawal right. Changes to withdrawal rights could cause the gifts to the trust to not qualify for the annual gift tax exclusion, and the grantor will be considered to have made taxable gifts.

Insights and Caveats

Fiduciary or not? Some state statutes provide that the trust protector owes a fiduciary duty to the beneficiaries, while other states seem to shield a trust protector from fiduciary liability for his or her actions or inactions. Additionally the trust document itself may state whether a fiduciary duty is owed or not. The extent to which a trust protector should or should not be considered a fiduciary and the implications of each on the operation of the trust have been the discussion of numerous recent commentaries. If the trust protector is considered a fiduciary, the extent to which the trustee will be held liable for directed actions of the trust protection may cause concern. Even if the trust document explicitly provides that a trustee will not be subject to such liability, this may not offer full protection to a trustee.

Conflict between Trustee and Protector. If a trust protector is given a power to veto a trustee's actions, an impasse for trust decisions could result. This may lead to decision-making on the trustee's part in order to avoid conflicts with the trust protector. If in addition to the power to veto a trustee's decision, the protector is also given the power to remove a trustee, a dissenting trustee may find that he or she is faced with no other

choice than to conform to the protector's direction in order to avoid removal. The above issues may support for the use of a trust protector in a limited capacity.

Drafting Suggestions. Commentators have suggested the trust provisions be drafted to delineate authority and liability between the trustee and the trust protector. Also, it is prudent to consider trust protector succession provisions.



DH Financial & Insurance Services

David A. Hjorth, CLU®, ChFC®, AEP®
Nicholas D. Hjorth, CPA, CLTC

Phone: (909) 981-4951
Fax: (909) 981-2768

Email: david@dh-financial.com
nick@dh-financial.com

Website: <http://www.dh-financial.com/>

David A. Hjorth and Nicholas D Hjorth, member agents of The Nautilus Group®, a service of New York Life Insurance Company. David A. Hjorth, CLU®, ChFC®, AEP® and Nicholas D. Hjorth, CPA, CLTC are Registered Representatives offering securities through NYLIFE Securities LLC (Member FINRA/SIPC), a Licensed Insurance Agency, 414 N. Second Ave, Suite C, Upland, CA 91786, (909) 981-4951. Financial Advisers offering investment advisory services through Eagle Strategies LLC, a Registered Investment Adviser. DH Financial & Insurance Services is not owned or operated by New York Life Insurance Company or its affiliates.

This tax related discussion reflects an understanding of generally applicable rules and was prepared to assist in the promotion of marketing of the transactions or matters addressed in this material. It is not intended (and cannot be used by any taxpayer) for the purpose of avoiding any IRS penalties that may be imposed upon the taxpayer. DH Financial & Insurance Services as well as New York Life Insurance Company, its agents and employees may not give legal, tax or accounting advice. Please consult your own professional advisors before making any decisions.

This information was produced by New York Life Insurance Company and provided as a courtesy by David Hjorth and Nicholas Hjorth. © 2016 New York Life Insurance Company. All rights reserved.

David A. Hjorth and Nicholas D. Hjorth, CA Insurance Licenses #0435847 and #0E08770