

Having served as an expert consultant / witness in trust litigation matters since 2013, I have observed seven “risk mitigation” strategies that a prudent trustee will adopt.

1) **Compliance Library:**

- a. CPC §16040: The trustee shall administer the trust with reasonable care, skill, and caution under the circumstances that a prudent person acting in a like capacity would use for a trust of like character with like aims to accomplish the purposes of the trust as determined from the trust instrument.
- b. Governance 101:
 - i. Policy = Statutory duty (This is your job description)
 - ii. Procedure = Workflow to prove the policy was followed
 - iii. Practice = Memo/writing that demonstrates the procedure was followed
 - iv. Compliance Library: Vault into which all memos/work product are filed
 - v. Compliance Calendar: Defining frequency of governance activity

2) **Annual Account:**

- a. CPC §16063: The trustee shall account at least annually, at the termination of the trust, and upon a change of trustee, to each beneficiary to whom income or principal is required or authorized in the trustee’s discretion to be currently distributed.
- b. CPC §16069(b) & §15800(b): In the case of a revocable trust, if no person holding the power to revoke the trust is competent, the trustee’s duties to account shall be owed to those beneficiaries... whom the trustee would be authorized to distribute income or principal to if the settlor had died during the account.
- c. CPC §16460: If a beneficiary has received an interim or final account or other written report that adequately discloses the existence of a claim against the trustee for breach of trust, the claim is barred as to that beneficiary unless a proceeding to assert the claim is commenced within three years after receipt of the account or report.
- d. The Annual Account is NOT a court accounting with the formality of CPC §1060.

3) **UPIA Matters - Manager Selection, Delegation and Monitoring:**

- a. CPC §16052(a): A trustee may delegate investment and management functions as prudent under the circumstances when selecting an agent, establishing the scope and terms of the delegation, and monitoring the by periodically reviewing the agent's overall performance and compliance with the terms of the delegation.
- b. Why did you select them? / What did you tell them to do? / Did they follow your instructions?
- c. A manager drafted IPS does not fulfill these three distinct duties of care.
- d. On benchmarking: There is no such thing as a perfect benchmark. A benchmarking study is designed to test if the manager was the in the "strike zone" for risk and return.

4) **UPIA Matters - Trust Stress Test:**

- a. CPC §16047(b): A trustee's investment decisions must be evaluated as part of an overall investment strategy by taking into consideration risk expectations and the needs for liquidity, regularity of income, and preservation or appreciation of capital.
- b. The Stress Test:
 - i. +Trust Income
 - ii. -Projected distributions and disbursements = X
 - iii. =Income Shortfall (if any) = Y
 - iv. Bond Bunker & Cash = Z
 - v. Distribution Coverage Ratio: Z / X
 - vi. Shortfall Coverage Ratio: Z / Y

5) **Trustee Compensation:**

- a. CPC §15601: If the trust instrument does not specify the trustee's compensation, the trustee is entitled to reasonable compensation under the circumstances.
- b. CRC 7.776
 - i. Gross income of the trust
 - ii. Success or failure of the administration
 - iii. Trustee's skill, expertise, and experience

- iv. Fidelity or disloyalty shown by the trustee
- v. Amount of Risk and responsibility assumed by the trustee
- vi. The time devoted to the trustee's duties
- vii. The custom in the community for Courts
- viii. The custom in the community for Corporate Trust companies
- ix. Did the work require more than ordinary skill or judgment

6) **Notice of Proposed Action:**

- a. CPC §16050 & §16053: A trustee may give a notice of a proposed action or a decision to not take an action. A trustee is not liable to a beneficiary if the trustee does not receive a written objection to the proposed action from a beneficiary within the applicable period (45 days).
- b. To sell or not to sell Grandma's house or Grandpa's low basis stock?

7) **Unreasonable Delay:**

- a. Duty to administer promptly and efficiently: To the extent the trustee is dilatory or inefficient in the administration of the trust, he is in breach of trust in that he is interfering with the beneficiary's property rights, the equitable interest itself being an interest in property. (Loring and Rounds – Duty to administer promptly and efficiently: 6.2.8)
- b. The Wave: There are 90m Americans who were born before 1965 (70m Baby Boomers and 20m Silent Generation). This cohort holds \$85t in assets (4x the US GDP). In the next 20 years, 2/3 of this cohort will be dead and their estate/trusts will need to be settled. And there aren't enough T&E attorneys in the US to do all this work.
 - i. As applied to CA: 7.2m trust/estate to settle in the next 20 years (CA = 12% of US population) representing \$14t in assets (17% of US wealth).
 - ii. Big Trusts in CA: 20% of the trusts/estate (1.4m) represent 80% of the assets (\$11t) = \$8m average and there are 10,000 T&E attorneys in CA. You each will need to settle 1 "large trust" every other month for the next 20 years.

8) **E&O Insurance (not risk mitigation, but risk shifting)**

- a. CPC §16240: The trustee has the power to insure the trustee against liability with respect to third persons.
- b. Cost of Defense + Indemnify Loss + Retention Rate
- c. Underwriting is, for the most part, bad and does not take into consideration the particular risk of a particular trust. (Premium range in the 0.10% - 0.30% of Trust/Estate per year)
- d. Check your group E&O policy for “excluded activities”. Are any of your partners serving as trustees on big, high-risk trusts?

9) **Anodos Services:**

- a. Settlement Facilitator: “Twice as fast at half the cost”
 - i. The CPA/attorney should do that which only they can do. We do the rest.
 - ii. \$3,000 per \$1.0m one-time fixed fee
- b. Trustee Governance Support: “Develop and maintain the governance process”
 - i. \$1,000 per \$1.0m per year
 - ii. \$12,000 minimum annual fee
- c. Trustee Compensation Study: “What does reasonable mean in this case?”
 - i. \$7,200 fixed fee
- d. Manager Audit: “Is the investment manager as good as they claim to be?”
 - i. \$7,200 fixed fee
- e. Annual Account: “If the CPA won’t do it, we will.”
 - i. \$300 per \$1.0m with a \$3,000 minimum annual fee

- ✓ DUTY TO HAVE A PLAN
- ✓ DUTY TO CONSIDER PREVAILING FACTORS
- ✓ DUTY TO MONITOR RISK/RETURN
- ✓ DUTY TO DIVERSIFY
- ✓ DUTY TO PAY FAIR FEES
- ✓ DUTY TO PRUDENTLY DELEGATE

ANODOS HELPS TRUSTEES DO THEIR DUTY WITH EXCELLENCE

TRUSTEE COMPENSATION

GRANTOR TRUSTEE GRANTOR

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TECHNOLOGY HAS CHANGED.
WHY IS PRODUCING THE ANNUAL ACCOUNT SO HARD?

ARE YOU ABLE TO INDEPENDENTLY VERIFY THAT YOUR MANAGER IS AS GOOD AS THEY SAY THEY ARE?

60 MILLION TRUSTS/ESTATES TO SETTLE IN THE NEXT 20 YEARS

TRUST/ESTATE ADMINISTRATOR OLD TRUST/ESTATE ADMINISTRATOR