TRUST & INVESTMENT

UPDATE

PremierBank
Here. For You. Always.

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A guide to our trust services

Why do so many financially successful individuals and their families look to trust institutions to meet their financial management needs? Several reasons come to mind:

- Trusts offer unique benefits in comprehensive wealth management.
- We provide a team approach, a fully staffed department with individuals who bring a diverse range of skills to the job.
- Our services are fee based—we are not compensated by generating transactions or through commissions for the sale of particular products.
- We are a corporate fiduciary, authorized by banking regulators to act as a trustee for individuals and institutions in the management and distribution of their assets.

What can be accomplished with this power to delegate the authority to manage property in a trust? Trusts can be individually tailored to address many different financial goals. As a result, there's no such thing as a "typical trust." See "Common Trusts, Uncommon Benefits" on page 2 for more details. All of these trusts have something in common. They have assets that require careful management, and that job falls to the trustee.

Essentials of every trust

The creator of a trust is customarily called the grantor. The grantor works with an attorney to prepare the trust agreement, which will give the trustee the instructions about the management of the trust and the distribution of income and principal. Every trust has beneficiaries, for whose protection the trust has been created. The grantor may be the first and foremost beneficiary of a revocable living trust—or the grantor and spouse. Otherwise, other heirs are named, whose interests will vest at various times, as specified in the trust agreement. If the trust is revocable, the grantor may amend it at any time, even terminate it. If the trust is irrevocable, such as a trust created at death by a will, it normally cannot be changed without court proceedings.

Finally, there must be a trustee. That could be an individual or a corporate fiduciary, such as us.

When should you consider a trust?

Trusts offer advantages in wealth management that are not available with ordinary investment accounts. Trusts can be used to achieve some or all of the following objectives:

- Provide lifetime financial protection for a surviving spouse.
- Establish inheritance management for minors, and incapacitated or disabled family members.

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- Protect assets from creditors.
- Reduce or eliminate death taxes.
- Increase financial privacy and confidentiality regarding wealth distribution.
- Implement a program of philanthropy.
- Protect an estate plan from claims by disgruntled heirs.
- Provide complete financial management in the event of your own incapacity.

Whatever the reason for creating your trust, the next question is crucial: Whom should you choose as your trustee? Who has the qualifications to see to it that your trust plan will succeed? Where would you look for the right trustee?

Who should be your trustee?

Typically, a trust grantor is deciding between a corporate fiduciary (a company that has been granted the legal right to act as a trustee, such as us) and an individual, such as a family member, friend, or business associate. Factors that should be considered include:

Judgment and experience. Inexperienced trustees may dissipate the trust assets, or make administrative mistakes that result in delays or other problems.

Impartiality. A trust typically has current income beneficiaries and future or remainder beneficiaries. The interests of both types of beneficiaries must be balanced carefully. Conflicts need to be resolved by a trustee that all the beneficiaries can respect.

Investment sophistication. The Uniform Prudent Investor Act and other laws governing the investment of trust assets must be adhered to. The trustee should be able to increase returns or reduce portfolio volatility, and must be able to diversify the portfolio.

Permanence and availability. Many trusts are expected to last a decade or more. Corporate trustees have the advantage of perpetual existence.

Sensitivity to individual beneficiaries' needs. Understanding the individual needs of trust beneficiaries is very important, and on this issue some people may assume that the friend or family member has the advantage. This is not necessarily the case, but sometimes an individual will be made cotrustee to handle such decisions. Even so, a corporate trustee might be brought into the process for an objective voice and to prevent unreasonable distributions.

Accounting and recordkeeping. Detailed trust records are required, and few individuals are equipped to handle this chore properly.

Fees. There is a chance that the fees charged for trust administration will be lower when a friend or family member is named as trustee. However, when a trustee is serving for little or no compensation, it becomes hard to give the trust the attention that it deserves.

In the usual case, the trust assets consist of ordinary investment assets, such as stocks, bonds, or mutual funds. In that situation, a corporate trustee is likely to be a very cost-effective alternative.

Would you like to know more?

The central features of today's trusts are professional asset management, conducted under fiduciary safeguards, in a segregated vehicle, which is bankruptcy-remote from the manager. This is what we do. How could a thoughtful trust plan improve the financial security of you and your family? We'd be pleased to explore that important question with you in more detail at your convenience. ☐

Common trusts, uncommon benefits

Type of trust	Beneficiary	Tax benefits?	Comment
Revocable living trust	Grantor, possibly grantor's spouse	None	Provides professional asset management, continuous financial protection upon incapacity. Avoids probate in many states.
Marital deduction trust	Surviving spouse	Full estate tax deferral in most cases	Spouse must receive all trust income at least annually, may direct ultimate distribution of trust assets.
Qualified domestic trust	Surviving spouse who is not a U.S. citizen	Full estate tax deferral	Spouse must receive all trust income.
Qualified terminable interest property trust (QTIP trust)	Surviving spouse and children	Full estate tax deferral	Especially appropriate for "blended families." Children's interests normally can't be changed by spouse.
Bypass trust	Anyone, but usually family members	No federal estate tax, possibly for decades	Limited to $12.06 million in 2022.
Spendthrift trust	Usually children, including adult children	None	Trust assets are protected from the beneficiary's creditors.
Special needs trust	Disabled individual	None	May provide for enhanced quality of life while permitting continued government benefits.
Charitable remainder trust	Grantor and/or family members, and a charity	Income, gift and estate tax deductions	Income interest may be a percentage of the trust's value or a fixed dollar amount.
Dynasty trust	Descendants	Avoid future estate taxes	Trust may last for 100 years or more.

The long-term investment perspective

"In short, bad news is an investor's best friend.
It lets you buy a slice of America's future at a marked-down price."

—Warren Buffet

That observation by the "Oracle of Omaha" was made 14 years ago, as the "Great Recession" was getting underway. We did not know then just how bad it would become. There is much worry today among investors that another recession might be on the horizon, given the struggles the Fed has had in trying to bring inflation under control. Stock market indices entered bear market territory earlier, but have since recovered somewhat, suggesting a return of optimism.

Although it may be true that recessions bring the opportunity for bargain hunting for stocks, they are not so easy to live through. Take Bill and Ted. As 2007 began, they each invested $1 million, Bill in large-capitalization stocks and Ted in long-term government bonds. For purposes of this example, we draw from the data in Kroll's 2022 SBBI® Yearbook, but note that you cannot invest in an index.

The first year for both investors was great, but then stocks crashed in 2008. Here's the score:

TWO INVESTMENT STRATEGIES

	Bill (stocks)	Ted (bonds)
2007	$1,000,000	$1,000,000
2008	$1,055,141	$1,099,024
2009	$664,612	$1,383,543

Source: M.A. Co.

Now what should these investors do? What if Bill panics, and switches to Ted's successful bond strategy? Unfortunately, that would mean he bought bonds at their high point. He would have been better off sticking with his stock investments, even though he would not get back to his original investment until 2013. Switching to bonds delays that moment until 2020.

TWO PATHS FOR $664,612

	Switch to bonds	Stick with stocks
2009	$664,612	$664,612
2010	$565,457	$840,415
2011	$623,074	$967,240
2012	$791,237	$987,674
2013	$820,046	$1,145,962
2014	$719,550	$1,517,029
2015	$897,093	$1,724,619
2016	$891,733	$1,748,297
2017	$907,142	$1,957,509
2018	$964,090	$2,385,015
2019	$958,060	$2,280,247
2020	$1,075,305	$2,998,378
2021	$1,254,188	$3,550,114
2022	$1,186,521	$4,568,926

Source: M.A. Co.

If Ted stuck with his bond strategy, his portfolio would have grown to $2,470,014 by the start of 2022. That's a bit more than half of the total return from large-cap stocks during the period. Interestingly, had Ted switched to an all-stock investment posture as 2009 began, he would have left the bonds at a high point and bought stocks at a low. By 2022 his portfolio would have grown to over $9.5 million! Just as Mr. Buffet suggested, the future of America was on sale.

All this goes to show is that hindsight is always 20-20. The factors that led to the Great Recession have little in common with today's economic headwinds—persistent inflation, pandemic hangover, energy shortages, and international instability with a hot war in Europe and growing tensions in the Pacific. In the short term, financial markets remain hard to forecast, given the uniqueness of this set of problems.

What about your investment portfolio? Are you confident in your investment strategy? Would you benefit from insights from our investment professionals? We'd be pleased to arrange a meeting at your convenience to discuss your objectives, concerns, and resources. ☐

Document those charitable gifts

The rough doubling of the standard deduction by 2017's Tax Cuts and Jobs Act has led to a dramatic decline in the number of taxpayers who itemize their deductions, which was the hoped-for result of the legislation. Overall, the IRS reports that for the 2019 tax year, only 11.1% of tax returns had itemized deductions, and only 9.1% of tax returns claimed a deduction for charitable gifts. However, the charitable gifts that are claimed now tend to be large, and so they need to be carefully documented. In particular, for gifts larger than $250 a "contemporaneous written acknowledgment" (or "CWA") must be provided by the charity to the donor. The CWA must include (i) the amount of cash and a description (but not value) of any property other than cash contributed; (ii) whether the donee organization provided any goods or services in consideration, in whole or in part, for any such property; and (iii) a description and good-faith estimate of the value of any such goods or services. Deductions for donations of property worth more than $5,000 must be accompanied by a qualified appraisal of the value of the property.

Recent case. Martha Albrecht and her late husband collected Native American jewelry and artifacts during their marriage. In December 2014, Martha donated 120 items from their collection to the Wainwright Museum of the American Indian. She executed a deed of gift, making clear that the gift was unconditional and irrevocable. On her 2014 tax return, Martha claimed a deduction of $462,676 for the value of her donation.

The IRS disallowed the entire deduction because Martha had not included the required CWA from the museum, confirming that she had not received any goods or services in exchange for her donation. The deed that Martha executed did not state that it was the entire agreement, and it was silent on whether goods or services had been exchanged for the donation. Although the museum later confirmed that there had been no quid pro quo, that was too late. Martha took her case to the Tax Court, which was sympathetic. "We appreciate what appears to have been a good-faith attempt by petitioner to substantially comply with the Code by executing the deed with the Wheelwright Museum," wrote the Court. However, the documentation requirements for charitable donations are very strict, and substantial compliance is not sufficient. Martha lost her case and her deduction, though her attorney said he planned to appeal.

Although recent tax law changes have simplified tax return filing for millions of taxpayers, taxes are more complicated than ever for those in the upper income brackets. Professional tax supervision is an essential service for the wealthy, especially for any plan of significant charitable giving. ☐