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ADMINISTRATION OF TRUST

The purpose of this memorandum is to discuss some basic issues in the administration of an irrevocable trust and to provide some guidance regarding the duties of a trustee. Please remember that this is a summary only. It cannot cover every possible issue that might arise in connection with the administration of the trust. An irrevocable trust may either be created in a separate trust agreement, or in a Will (a "testamentary" trust).

A trustee is generally charged with administering the trust for the benefit of the beneficiaries. That involves taking possession of trust assets, seeing that they are properly invested, and making distributions in accordance with the trust instrument. Because the trust is a separate entity and often a separate income taxpayer, it is important that the trustee keep detailed records to account for the principal, income and distributions of the trust. Not only are beneficiaries entitled to be kept informed about the trust administration, but there are filings the trustee must make on behalf of the trust.

1. **Possession of Trust Assets**. The trust should be funded as provided in the trust instrument or Will. Assets owned by the trust should be titled in the name of the trust, and the trustee is the one authorized to sign on behalf of the trust. The trust's taxpayer identification number should be used on all accounts owned by the trust. Different states have different rules for titling real property in the name of the trust. In Colorado a deed to the name of the trust (not the trustee) is recorded, together with a Statement of Authority indicating the identity of the trustee. When a bank account or investment account is opened in the name of the trust, a Certification of Trust should be provided to the company.

2. **Investment Responsibilities**. A trustee has the duty to invest trust property in a prudent manner. Under Colorado's Uniform Prudent Investor Act, a trustee is entitled to consider whether the portfolio as a whole is prudent, instead of looking separately at each individual investment. When considering trust investments, a trustee should keep in mind the needs of the beneficiaries with respect to production of income and preservation of principal. A trustee is also required to diversify trust investments, unless there is a reason not to diversify under the circumstances. Generally, trustees are fairly conservative in their investments, and should not invest in speculative schemes. Even though a trustee may employ an investment advisor, the trustee still has a duty to monitor the investments.

3. **Trust Accounting**. The trustee has a duty to keep proper records of all receipts, expenses and distributions for the trust. Under the trust terms, and also under Colorado law, the trustee has a duty to account for trust transactions to the beneficiaries. To simplify the preparation of this accounting, the trustee should open an interest bearing account in the name of trust, and channel all trust receipts and expenses through this account. The trustee should be sure to write down a complete description of each entry. Generally, the "qualified beneficiaries" must be given at least an annual accounting listing receipts and disbursements, and a schedule of assets as of the end of the year. "Qualified beneficiaries" include the current beneficiaries and the first level of remainder beneficiaries. The qualified beneficiaries must also receive a copy of the trust provisions affecting their interests.

4. **Terms of the Trust**. The trustee has a duty to administer the trust under the trust terms for the benefit of the beneficiaries. The particular terms of the trust are the guidelines for all distributions and the identity of beneficiaries, and most be closely followed.

5. **Power Regarding Accounting Adjustments**. Many trusts give the trustee discretion in making distributions of income and principal to the beneficiaries. If the trust instrument requires net income only to be distributed to a beneficiary, and the trustee is not given the discretion to also distribute principal, then Colorado law generally gives a trustee certain powers to adjust between income and principal, if necessary, to be fair to all of the beneficiaries. Colorado law also gives a trustee the power to convert an income-only type trust to a unitrust, if appropriate. The powers to adjust and convert to a unitrust are complex, and should be discussed with counsel if applicable.

6. **Income Tax Matters**. A trust reports income on a calendar year (the only exception is a revocable trust that elects to be taxed as part of the estate on a fiscal year). The income tax returns are due April 15 of each year, unless extensions are requested. If the trust is a separate taxpayer, a taxpayer identification number must be obtained from the Internal Revenue Service. That

number should be used on all accounts in the name of the trust. Even though income tax returns must be prepared and filed for the trust each year, there may not be any tax to pay if the entire net income is distributed each year to the beneficiaries. Generally, a trust pays tax only on income it retains, and the beneficiaries pay tax on the income they receive.

In addition, under Code §678, if a trustee has the power exercisable solely by himself or herself to vest trust principal or income in himself or herself, then that trustee will be taxed on the trust's income, whether or not it is actually distributed by the trustee. There are other provisions that may cause a trust to be a "grantor trust" and be taxed as if all the income is reported on the individual return of the grantor. These issues should be discussed with your accountant.

7. **State Law Matters**. A trustee has a "fiduciary" duty to properly administer the trust. This means that the trustee has a duty to follow the trust terms, and to protect the interests of the beneficiaries. As mentioned above, the trustee must keep the qualified beneficiaries informed, such as by providing them with an accounting each year. Colorado's version of the Uniform Trust Code "UTC" requires a trustee to send a Notice to all "qualified beneficiaries" of the trust, advising them of the existence of the trust and the acceptance of the appointment of the trustee. The Notice must be sent 60 days after acceptance of the trustee. A trust registration statement may be filed with the court where the trust is administered, if it is administered in Colorado, but under the UTC this is optional instead of mandatory. Unless court consideration of a particular matter becomes necessary in the future, the court will usually not have any further involvement with the trust.

8. **Trustee Powers**. The trust agreement or Will usually contains a specific list of trustee powers. In addition, a list of general powers under Colorado law can be found in the Colorado Fiduciaries' Powers Act, at C.R.S. §15-1-801, et seq. and in C.R.S. §15-5-815 of the UTC. Generally, the trustee of a trust can take whatever actions necessary to properly administer the trust, consistent with the terms of the trust and the fiduciary relationship.