FEATURE:
FIDUCIARY PROFESSIONS

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Letting Go of the Dead Hand: Part II

With silent trusts, all might not be quiet on the western front

This article is the second in a series considering the downsides of trustor's dead hand control in trust planning. In the first article, we addressed the challenges and limitations of traditional trust planning.[1] We'll now address the downsides of the relatively new phenomenon colloquially referred to as "silent trusts" or "quiet trusts."

As trust laws have evolved, we can now draft trusts that eliminate a beneficiary's right to get any information about a trust completely for long periods of time. Generally, fiduciaries have a duty to notify and inform beneficiaries about the existence of the trust, provide them with basic information like account statements and respond to inquiries.[2] Silent trusts generally require someone to serve as a "designated representative" to stand in the place of the beneficiaries, as their proxy, to receive account statements and information, consent or sign releases and generally act on behalf of the beneficiary who's prohibited from receiving information about the trust, in all of the ways that a beneficiary would ordinarily interact with the fiduciaries and represent their own beneficial interests in the trusts.[3] The need to appoint and replace a designated representative who will always be there to serve while the trust is silent can create a complicated structure. Furthermore, it's often difficult to identify someone who's willing to step into a fiduciary role and take on potential liability when they bind the beneficiaries and essentially shift the spotlight of fiduciary risk off of the trustee and onto themself.




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The Conversation

Silent trusts are a major trend right now, driven primarily by settlors' fears that their children and other descendants might become lazy and unproductive "trust fund babies" or that access to large amounts of wealth might become harmful to them. Because the silent trust option is readily available in many trust jurisdictions, it appears to offer an easy, ready-made solution for that fear. The conversation often goes like this:

> The client says, "I am really concerned about my children becoming trust fund babies."
> The attorney says, "Well, we could draft this as a silent trust so that your children do not get account statements and don't know about the trust. Would you like to do that?"
> The client immediately says, "Yes! That sounds good!"

The client's response to a silent trust is almost always going to be "yes" when it's posed this way—without additional discussion about all of the nuances and potential downsides of a silent trust. But what are we *really* doing with silent trusts? Are we trying to give the beneficiaries an artificial sense of scarcity with secrecy and deception, followed by the eventual BIG reveal? What kind of message does a silent trust

send to the beneficiary? Isn't it ultimately interpreted by the beneficiary as a clear message of distrust and a lack of faith and confidence in the beneficiary? Silent trusts may be appropriate in certain circumstances, especially with young beneficiaries, beneficiaries with special circumstances or while the grantor is alive to prevent children from anticipating their inheritance before its time.[4] But the conversations we have with clients about silent trusts rarely play out the scenarios of what will *really* happen with a silent trust. Planning conversations rarely explore the details of how a trustee will end up administering a trust that's shrouded in secrecy with a framework of other individuals representing the beneficiaries, how situations will be handled when some beneficiaries inevitably find out about the trust's existence before they're entitled to know anything about the trust (including its very existence) and how that will ultimately impact the beneficiaries' relationship with the trust and inherited wealth and the feelings that all of this might generate toward the trustor.

Common Problems

Some of the common problems with silent trusts include:

1. Beneficiaries who aren't entitled to know about the trust will inevitably find out about the trust. We all know it's impossible to keep this type of secret in a family. How should the trustee handle beneficiaries who find out about the trust before the trustee is permitted to communicate with them?
2. How will the trustee effectively evaluate the distribution needs of the beneficiaries, which is integral to the beneficiary's interest in the trust?
3. How does the trustee go about actually making distributions to or for the benefit of a beneficiary who doesn't know about the trust?
4. How does the trustee keep the existence of the trust from the beneficiary when fulfilling tax reporting (K-1s) associated with distributions?
5. How do you identify a designated representative willing to take the fiduciary risk, and how do you ensure that you have a designated representative in place in perpetuity, especially when the trustee won't want to appoint the designated representative, and many or all of the beneficiaries of the trust won't know about the trust?
6. Who will have the power to remove and replace the trustee, trust protector or other advisors, and how do you ensure someone holds that power at all times?
7. How do you handle beneficiaries who possess *Crummey* withdrawal rights?
8. How do you keep the existence of the trust from a beneficiary if there's litigation involving the trust or the trustee, or some other party must institute a court proceeding or seek judicial instructions?

There are numerous silent trusts being created today, and it's likely that many of those trusts will encounter one or more of these problems.[5] Planners who jump right into silent trusts to try and appease a client's fear without discussing the impact on beneficiary growth and well-being and the administrative obstacles to accomplishing the objective are just whistling past the graveyard.

From a trustee's perspective, silent trusts are problematic for a number of reasons.

Trustee Issues

Silent trusts, especially those that remain quiet after the grantor's death, represent the antithesis of the beneficiary well-being approach we favor. The object of a good trustee is to build trust and a long-term relationship with the beneficiary. Silent trusts require the trustee to administer a trust shrouded in secrecy—tainted by mistrust from the start.

The trustee can't exercise its discretion except in a vacuum—which could be filled with an unconscious bias against a beneficiary whom the settlor distrusted with information critical to the beneficiary's own well-being. A silent trust prevents collaboration growth between the trustee and beneficiary and

blunts an opportunity for financial education and maturity through this partnership.

As outlined above, silent trusts place the trustee in an almost untenable administrative position. The numerous practical obstacles to silence require extremely detailed, precise drafting of the gymnastics a trustee must endure to ensure silence even in the face of: *Crummey* notices, disguised beneficiary distributions ("Where'd THAT money come from???"), K-1s, trust distributions to other beneficiaries, petitions to amend the trust, etc. The result is a complicated structure that will be difficult to maintain in the name of avoiding what's probably unavoidable inadvertent disclosure.

When the beneficiary does inadvertently discover the existence of the trust, the trustee *may* be legally protected, but the relationship with the beneficiary likely will be poisoned, the silence having irreparably created suspicion of impropriety. There's always a chance, however, that the trustee will be exposed to liability for negligently revealing the existence of the trust.

Finally, there's the question of whether the reports provided to a surrogate standing in the beneficiary's shoes will start the statute of limitations to run for claims against the trustee. In certain states, the statute won't begin to run until many years later when the beneficiary receives information adequately disclosing the breach. Statute of limitations concerns may work against the beneficiary, too, as some statutes begin to run when a trustee resigns, which may have occurred many years before the beneficiary learns of the breach. In that case, it's the beneficiary who will be out of luck.

These issues become more pronounced the longer the duration of the silent period is. What may be reasonable for a beneficiary still in college or young adulthood quickly becomes absurd and difficult to maintain as the beneficiary ages.

Not all states permit silent trusts, but that doesn't stop clients from demanding that the trustee withhold information. The trustee's nightmare is the client who demands that the trustee withhold information from the beneficiary even if state law—or the trust instrument—provides otherwise. This places the trustee in a very difficult position: Please the client, or follow the law and risk the relationship. While trustees can't cure what may be the generations of dysfunction that may be behind the settlor's desire for secrecy, our experience leads to the conclusion that in almost every circumstance, communication, cooperation and collaboration between the trustee and beneficiary will lead to a better outcome for the beneficiary.

Silent trusts can rob the rising generation of valuable teaching moments and meaningful dialogue.

Rising Gen Perspective

Silent trusts might appear to maintain an air of quiet stability. However, from the rising generation's perspective, this silence can be a deafening problem. Keeping secrets about a beneficiary's interest in a trust doesn't make the wealth go away, and eventually it will make an appearance in the beneficiary's life. Often the beneficiary will begin hearing about the trust's existence and the family wealth from other beneficiaries or even outsiders. While parents may have concerns about the beneficiaries' maturity and ability to process financial responsibilities, the rising generation often will craft their own narratives, and these often lean towards the negative. It's often preferable for the parents to lead the narrative on money from an early age and prepare the beneficiaries to handle what's eventually coming their way instead of hiding it from them, hoping they'll be ready when reality becomes revealed.

Silent trusts can rob the rising generation of valuable teaching moments and meaningful dialogue. A silent trust prevents beneficiaries from observing decisions being made, understanding why they're made and developing financial competence and confidence. The most valuable source for this knowledge is generally the settlor who generated the wealth and set an intention for how it would be administered for their benefit. The implications go further. They also deprive the current generation of the opportunity to tap into the unique perspectives of the rising generation, especially in areas such as technology, diversity and inclusion, impact and sustainability and how the rising generation can best be served. The trust can become a platform for

guided communication, collaboration and confidence-building for the rising generation. Enterprising families in particular require more communication than your average family because of the complexities and challenges they face. Collaboration can often be most beneficial, yet a silent trust acts as a wall that blocks a family's potential rather than a bridge connecting generations and fostering a culture of openness and development.

Driving Force: Fear

If silent trusts make the drafting attorney's job more complex, the trustee's job more difficult and the beneficiary's engagement and education impossible, why have they perpetuated? The driving force behind planning techniques such as silent trusts is fear. Wealthy parents—like all parents—want the best for their children. Wealth can feel like a complicating factor to this goal, especially in the context of the deeply held narrative that wealth is a corruptive force. The belief that wealth is destructive has deep cultural roots and has been perpetuated by both wealth holders and their advisors alike (this is a hallmark of Wealth 2.0, an era in the wealth advising field that emerged in the 1970s and 1980s).[6] While there were many wonderful advances that emerged for families and their advisors during this era (such as the amplification of the voices and lived experiences of beneficiaries and the recognition that wealth often has a psychological impact on an inheritor's life), Wealth 2.0 also perpetuated advice and planning that was rooted in fear. The goal has been to protect beneficiaries from the assets, rather than educate them on how to engage with the assets in a meaningful and productive way.

But there's a better way. In our next article, we'll describe the way planners can discuss with their clients how to use transparency and communication to motivate and empower the rising generation and how trusts can be structured and administered to enhance beneficiary growth and well-being.

Endnotes

1. Niké Anani, Todd A. Flubacher, Kristin Keffeler and Philip J. Hayes, "Letting Go of the Dead Hand," *Trusts & Estates* (December 2023).
2. *See Restatement (Second) of Trusts* Section 173; *Restatement (Third) of Trusts* Section 173.
3. David A. Diamond, "The Administration of Quiet Trusts and Decanting Trusts," *Trusts & Estates* (September 2016).
4. *See* David A. Diamond, "Considering Quiet Trusts in the Larger Picture of Family Governance," *Trusts & Estates* (May 2022); Donald D. Kozusko, "In Defense of Quiet Trusts," *Trusts & Estates* (March 2004); Al W. King III, "Should You Keep a Trust Quiet (Silent) From Beneficiaries?" *Trusts & Estates* (April 2015).
5. *See* Robert Whitman, "Full Disclosure is Best," *Trusts & Estates* (July 2004).
6. James Grubman, Dennis T. Jaffe and Kristin Keffeler, "Wealth 3.0: From Fear to Engagement for Families and Advisors," *Trusts & Estates* (February 2022).

SPOTLIGHT

Mirror Image

Seated Figure (after, Study for a Portrait 1981) (S. 5, T. 15) by Francis Bacon, sold for £15,24 at Phillips Evening & Day Editions auction in London on Jan. 17-18, 2024. Known for his raw, often disturbing imagery, Bacon didn't start painting until he was in his late 20s. Many of his portraits of reclining figures, such as this one, include circular arrows to indicate rotations.