

# UNINCORPORATED BUSINESS ORGANIZATION and IRREVOCABLE TRUST MANAGEMENT

## DISCLAIMER

The information being offered here is purely educational and informative in nature and does not constitute professional, legal, or tax advice. You must take full responsibility for any liability or loss incurred as a consequence of the use and application, directly or indirectly, of any information contained in this pamphlet.

This concise educational booklet is a modest outline showing the Trustee's rights and obligations in the management of the trust. In order to accomplish the long range objectives for which this trust was created, it is mandatory that your administration of the trust be consistent with the rules of *fiduciary law* as set forth in the trust instrument and the common law.

As a foreword, it is the ambition of this booklet to inform the Trustee that much of what is done in the initiation and execution of estate planning falls under the umbrella of *fiduciary responsibility*. In some respects, it is difficult to define the word "*fiduciary*" from a technical standpoint. However, defining the term in practical reality and conduct is less difficult. In the simplest of terminology, the *fiduciary obligation* of a person acting as a trustee, executor, or one who holds other forms of authority to act under a power-of- attorney dictates that they function and conduct themselves in such ways as to maximize the benefit(s) for the person(s) whom they are serving. The concept of *fiduciary* is founded in ideas of integrity and reliance. The conduct of the *fiduciary* is measured in hindsight. Hence, *fiduciary* demands a high level of planning, research, and fidelity. *Fiduciary responsibility* may be the most onerous of all obligations imposed upon an individual under common law and the laws of the several States; its violations being punishable by lawsuits, imprisonment, fines, or all three.

Accomplishment of the *fiduciary responsibility* by trustees, executors, or those who receive powers to act in the name of others must be expressed in terms of absolute personal conduct which includes, at a minimum, the following:

(i) Adequate capability and time to perform the services required. One who accepts appointment as the Trustee will own the bare legal title, but the beneficial title - that is, the right to have utilization of the property - is vested in others for whom the Trustee is acting.

(ii) Proper counsel and guidance from legal, accounting, tax, insurance, investment, etc. on an on-going basis. Service rendered by the Trustee must be based on the highest degree of fidelity and principles of integrity. Failure to follow those may result in not only a loss to the beneficiaries, but may also result in significant liability to the Trustee.

(iii) Careful preparation and implementations of binding documents. The concept is for the fiduciary to recognize that, first and foremost, the responsibilities which he or she has undertaken require acting in the best interest of the beneficiaries for their health, education, maintenance, and support.

(iv) Maintenance of quality records and regular reporting. The practice of good, concise, record keeping should be of significant assistance to the family and all those assuming *fiduciary responsibility* within the family, by having clear records of existing documents fundamental to the implementation and administration of estate planning for the family.

(v) Available access to information and disclosure of all relevant documents and information to the beneficiaries on a regular basis. One of the most important requirements for quality estate planning is ready access to relevant information. This organizing should assist in producing, in a succinct way, a simple method of finding relevant information concerning the family, the underlying desires and goals of the family, the estate planning documents utilized and their implementation, and all financial assets and financial statements.

(vi) Preparation and filing of all reports, whether to institutions or government tax agencies. Important records and transactions are to be kept in the trust minutes. Accurate records of what you have done will make the tasks of your successor trustee(s) much easier.

The instructions outlined below are very general in nature and are drafted to assist you in answering questions you may have concerning the trust of which you are a Creator, and perhaps a Trustee, or even an enjoyer of beneficial interest.

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# STEP-BY-STEP PROCEDURES IN SETTING UP YOUR PURE EQUITY TRUST

This informational manual is strictly designed to aide you in the initial setting up, later on implementing, and then long range organizing and administration of your business trust operation. Every page and NOTE is important so please carefully read and understand your duties and requirements thoroughly before proceeding. Please read the following statement:

## **Trust Must Have Economic Reality and/or Business Interest!**

*The Creator expressly declares this to be an UNINCORPORATED 1041 Irrevocable Complex Contractual Organization business cast in the form of a Trust which is founded upon the freedoms and rights inherent in the common law of the Republic of these united States of America as set forth by **We The People** in the Constitution of the United States, the Bill of Rights, and the original state constitutions of the several states comprising (the union) of the United States of America. The Creator further declares that this contractual trust will always maintain an economic reality and/or a business interest.*

*However, IRS Regulation § 301.7701-4(b) states "There are other arrangements...which are often known as business or commercial trusts...which normally would have been carried on through business organizations that are classified as corporations or partnerships...[unless] if, applying the principles set forth in Sections 301.7701-2 and 301.7701-3, the organization more nearly resembles an association or a partnership than a trust." [Emphasis Added]*

*Section 301.7701-2(a)(1) clarifies the characteristics of corporations. It states "There are a number of major characteristics ordinarily found in a pure corporation which, taken together, distinguish it from other organizations. These are: (i) Associates, (ii) an objective to carry on business and divide the gains therefrom, (iii) continuity of life, (iv) centralization of management, (v) liability for corporate debts limited to corporate property, and (vi) free transferability of interest." The remainder of the Section says that "the organization [must] more nearly resemble a corporation than a partnership or trust." See IRS Revenue Ruling 75-258 and [Morrissey et al. v. Commissioner](#), (1935) 296 U.S. 344.*

*Section 301.7701-3(a) also defines the partnership as any group that "includes a syndicate, group, pool, joint venture, or other unincorporated organization...which is not a corporation or a trust or estate within the meaning of the Internal Revenue Code of 1954."*

*This trust seeks no privileges or benefits from any government or government agency, does not have associates, has been created for an ongoing business, expires after an arranged length of time, deliberately has centralized management in the form of an independent trustee, is totally liable to debts, and under no circumstances allows free transferability of interest. The trust has only three of the six characteristics and not a preponderance of those characteristics; and is certainly not a partnership or corporate "statutory trust," but a separate lawful entity having its existence under the common law.*

## **Installation of Your Irrevocable Trust**

You have taken the first important step in estate preservation planning. The trust instrument is the centerpiece of your estate plan. Treat it with care and attention and you will derive the intended results.

It is important to review all the documents that have been provided. The information herein will give you the foundation to install the trust entity in its entirety and to move forward in a simple, easy manner. Often there is a tendency to skim information to get a "flavor" of what is being said. Treating the trust information in this manner could cause you to miss an important step, or to not fully understand all necessary trust requirements. You will find that reading all information provided will answer most if not all of your questions. Please do not short cut this procedure.

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### **FIRST: WHAT'S IN THE TRUST PORTFOLIO PACKAGE?**

The trust portfolio package has been divided into fifteen (15) different Tabs (or sections). Each Tab is a uniquely different but vital part of the entire overall trust portfolio. No section of the trust can operate in and of itself. It is therefore important that the different parties involved in this trust portfolio carefully read and understand the different parts of this asset protection entity.

#### **Inside Table of content page:**

Table of Contents and a copy of "Final Instructions and Acknowledgment of Receipt of the Portfolio ..."

#### **Tab 1:**

The "Declaration of Trust Agreement" and "Memorandum of Declaration of Trust Agreement." This memo is for any third parties with a need to know what the powers of the trustees are and really has no other purpose. The SS-4 Form is an IRS form and its function is to acquire a Federal I.D. Number for the trust.

**Tab 2:**

1. The trust indenture: This is the “Deed of Trust” contract and declaration of the business trust that the creator/s, exchangor/s, and/or grantor/s have/has with the trustee/s to control the assets of the trust for the benefit of the beneficiary/ies. The document begins by declaring the “valuable consideration” that the principle/s exchanged with the trustee/s in exchange for beneficial enjoyment. The date of the declaration is acknowledged and the authority is given to the trustee/s to operate under the name the creator/s has/have given the trust. Finally, section 1 ends with the trustees’ acceptance of the trust. This is the most important document of any trust and should be read by the creator/s and all the trustees. The trust indenture lets all know just what the creator/s want/s the trustee/s to do, who is to benefit from the trust and in what amounts or quantities and how.

**NOTE:** Dispersed throughout the document are legal situs, informational boxes, footnotes, cautions, warnings. One should not take any of these additions for granted. They are there to assist all involved to do their task properly and legally at all times.

2. Schedule “A”: This is a list of all the real property placed into the trust by the creator/s, exchangor/s, and/or grantor/s. Whenever possible, this should be by each property’s legal description and/or parcel numbers.

3. Schedule “B”: This is a list of the personal property placed into the trust by the creator/s, exchangor/s, and/or grantor/s. The creator/s should fill out each section such as professional property, financial institutions, stock/securities, deferred compensations, insurances, business affiliations, and/or make an inventory and attach it to each section as required.

4. Schedule “C”: This is the certified list of the original certificate holders. They are the people who will benefit from the trust profits. They are called certificate holders because they own

Certificates much like stock in a corporation except they have no vote or say in the running of the trust or in its management. Actual certificate's with accompanying certificates evidencing the issuance (much like a certificate of authenticity) can be issued if the creator/s wish/es.

5. Schedule "C" Continuation: This is referred to as a "capital shares registry and transfer journal" which list the current certificate holders. They are the people who are currently benefitting from the trust profits. Again, they are called certificate holders and actual certificate's with accompanying certificates evidencing the issuance can be issued if the creator/s wish/es.

6. Schedule "D": This is a listing of the suggested successor unit of beneficial interest holders after the death of the current holders. The trustee/s is/are not required to comply with these wishes, only consider them when re-issuing the certificates after the death of a current beneficial enjoyment holder.

7. Schedule "E": This contains a list of the original trustee/s and his/her/their addresses. Successor trustees are recorded in Tab 4 by proper resignations, removals, and/or replacement letters. There is no need to record the current trustee/s here unless the record keeper of the trust so desires for convenience.

8. Schedule "F": This is a certified list of all excluded persons from becoming beneficial enjoyment parties to this trust.

9. Schedule "G": This is a listing of all person contracted by the trust who are empowered to remove, or have removed, trustee/s or other contracted persons.

10. Schedule "H": This listing will contain the names and addresses of any or all appointed "emergency trustees." Emergency trustees are not normal day-to-day involved trustees but there in case of the unforeseen removal of a trustee by death, resignation, removal, or incompetence.

11. Schedule “I”: This is where the trust protector’s name and address will be recorded. As with Schedule “E” above; replacements should be contracted and their contracts kept in Tab 7 and/or can be recorded here.

**Tab 3:**

The “Creator/s Letter/s of Wishes” are kept in this section.

**Tab 4:**

The appointment and affirmation letters of all trustees are recorded and maintained here by the trust record keeper.

**Tab 5:**

Trust minutes are filed in this section. The initial minutes are very important to the proper implementation of the trust agreement. One very special section is the Bank Resolution Minutes. This minute is designed especially for the Banks. The Board of Trustees sign this minute stating what bank is to be used and who will be the signatures on the account.

**NOTE:** It is easier to use a computer generated and controlled “minute and/or resolution” program therefore we recommend Trust Manager software. Trust Manager can be purchased by going to the internet and logging on to [www.trustsoftware.com](http://www.trustsoftware.com) , by calling toll free at 888-878-7860 or write to: TRUST SOFTWARE & CONSULTING, 5515 North 7th Street, Suite 5-324, Phoenix, AZ [85014].

**Tab 6:**

Every business trust has a day-to-day manager and he/she/they are contracted to the trust. This is where their contracts are recorded. This contract appoints trust managers and defines what are their duties, powers and limitations.

**Tab 7:**

If a trust protector was designated, this is where their contract would be located. The trust allows the creator/s to appoint a

protector. The protector's only power is to appoint and/or remove trustees "with cause". Some creator/s feel that the protector is necessary while other don't rely or want their services.

**Tab 8:**

Lease agreements and/or consignments agreement should be kept in this section.

**Tab 9:**

The trust may require the use of employees. Make sure that everyone, repeat everyone, who does anything for the trust is under "contract." Maintain all employee contracts in this section.

**Tab 10:**

The property deed legally conveys real property into the trust by the exchangor/s and/or grantor/s. In the trust package will be the old deeds as well as the new deeds made out to the trust. All deed should be maintained in this section for easy reference.

**Tab 11:**

Many people who establish business trust do so to maintain privacy in their affairs. The greatest loss of privacy today is through the extensive use of the social security number. The social security number (SSN) was NEVER intended to be used as a national identifier and Congress has passed registration to prohibit it being used as such. This constructive notice is designed to combat those who demand your SSN even though it is not required by law. Make copies and use it over and over again to protect your privacy.

**Tab 12:**

This section contains this article and a condensed version of our 40 plus page booklet entitled "Agency and Fiduciary Responsibility in the use of Wills, Trusts, and Partnerships." They are both MUST READS by anyone who wants to operate a proficient business trust arrangement.



**Tab 13:**

Trust accounting is so vital to the legal operation of an unincorporated business organization that we've included four different forms required if you're not using a computer software program such as Quicken Home & Business or QuickBooks. Make as many copies as you need to record trust income, expenses, asset acquisition and disposition.

**Tab 14:**

Please keep copies of all UBI Certificates and Accompanying Certificates Evidencing the Issue of UBI (much like a certificate of authenticity) in this section. Current as well as surrendered Certificates must be maintained for accounting purposes. Ensure that Schedule "C" Continuation of the trust agreement is current as well.

**Tab 15:**

This section has all kinds of Miscellaneous Supporting Documents included for your support in maintaining accurate and concise records. Some of these special documents are letters for stock transfers, change of ownership and beneficiaries of insurance companies, membership transfers etc.

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**SECOND: FURTHER DESCRIPTIONS OF TRUST PARTICULARS.**

**THE TRUST INDENTURE:**

The trust indenture, or agreement, consists of fifty (50) or so pages. As the creator/s, grantor/s, and/or exchangor/s read each page and pay special attention to the highlighted boxes and **NOTES**. The creator/s, grantor/s, and/or exchangor/s then sign and date the Acknowledgment page in the presence of a Notary Public.

The Creator/s then appoint/s and the First Trustee agrees to serve the trust in this capacity. This is done by using one of the Affirmation of

the First Trustee by the Trustee forms (Tab 4). Both the creator/s appointing the Trustee and the Trustee signs it accepting the trust.

Next the First Trustee can appoint the Second Trustee (Tab 4) but this time it is signed by the First Trustee doing the appointing and the Second Trustee doing the accepting.

**Both of this forms must be signed and dated.**

SCHEDULE “A”:

Schedule “A” is the list of the real property placed in trust by the Exchangor/s and/or Grantor/s. The property should be described on the schedule by property description just like on the deed. If there is not enough space on the face of the form for the description then pages may be attached to the back. This Schedule is an official document of the trust. This is where the Exchangor/s and/or Grantor/s deliver/s the real property into the trust and the Trustees accept them.

**This form must be signed and dated by all concerned.**

SCHEDULE “B”:

Schedule “B” is the list of the personal property placed in trust by the Exchangor/s and/or Grantor/s. The property should be described on the schedule generally and an inventory attached to cover the details. This Schedule is also an official document of the trust. This is where the Exchangor/s and/or Grantor/s deliver/s the personal property into the trust, and the Trustees accept them.

**This form must be signed and dated by all concerned.**

SCHEDULE “C”:

Schedule “C” is the certified list of the Certificate Holders; i.e., the ones that are to benefit from the trust. The Grantor/s and/or Exchangor/s is/are almost always the first Certificate Holder/s. Later he/she/they may want to give some of the UBI’s away to his/her/their child/ren and/or friend/s.

**The official document in the trust to record this transaction is Schedule “C” which must be signed by the Trustee/s.**

What are UBI's? The Units of Beneficial Interest (UBIs) of the trust are similar to stock certificates in a corporation but the UBI holders have no vote or say in how the Trustee/s operate the trust. They only have a right to receive income, if any is generated, from the trust provided the Trustees vote to distribute any dividend/s.

SCHEDULES “D” ~ “I”:

The remaining Schedules were described above. They are important accounts of people and entities involved, or not involved, with the trust. Refer to the first section for a more detailed description.

THE PROTECTOR:

The trust indenture does not allow the Creator/s, Grantor/s and/or Exchangor/s any control, influence, or dominion over the Trustees. The trust indenture does allow the Creator/s to appoint a Protector of their personal beneficial interest to watch over the behavior of the Trustee/s. The Creator/s do not have to utilize a Protector but sometimes it is wise to have. The Trustee/s do not sign the form but they should be informed of its existence before accepting as Trustee/s. **This form must be signed by the Creator/s and the Protector.**

SS-4 FORM:

This form is provided by the Internal Revenue Service and it is required to be filed by the Creator or trustee in order to obtain a Federal Identification Number. **This form only needs to be signed by one Trustee or the Creator.**

GRANT DEED:

The Grant Deed (in some states called a Warrant Deed) is the way property is legally conveyed. A new Deed is required to put real property into the Trust. Once the Deed/s has been signed and notarized it can be recorded at the County Recorders office. In California, if this is completed properly it does not result in a reappraisal for property taxes. **The Deed/s must be signed by the Grantor/s, and it must be Notarized.**

### BANK RESOLUTION MINUTES:

For the Trustees to set up a Bank Account; a meeting should be called and the matter of what bank, checking and/or savings accounts, who should be the signatories, how many signatures required etc. should be decided. Then a Minute should be drawn up reflecting their Resolution. **This should be signed by all involved.**

### THE MEMO:

This is just what it says, a memo. It is used to inform any third party (anyone not in the trust) of the powers of the Trustee/s. It can be used by banks, escrow companies, insurance companies, lawyers, courts etc. and any third party that needs to know the powers of the Trustee/s. **This memo must be signed and dated by the Trustee/s.**

### MANAGERS AGREEMENT:

Most Trustee/s do not have the time or specific skills required to manage the business purpose of the trust. They, and they alone, can appoint Manager/s or Caretaker/s of the trust. This person/s can have as little or as much power as the Trustee/s see fit to grant. He/she can sign on the bank accounts, rent property, make investments etc.; but the Manager/s cannot hold property in his/her/their name/s, only the Trustee/s can hold property. The Manager/s can only be appointed at a meeting of the Board of Trustees. This should be accomplished at the first meeting of the Trustees but it can be done at a later meeting. The Manager/s should be given a formal appointment letter or form (one has been provided if you want to use it). **This form must be signed and dated by the Trustees and the Manager/s.**

### SPECIAL LETTERS OR FORMS:

When you receive your trust packet there may be some letters for stock, insurance, membership etc. transfers. These must be signed and dated by the Exchangor/s and/or Grantor/s and sent to the companies involved so the transfer/s can be made. **Once the Exchangors/, Grantor/s and Trustee/s have signed all the forms and recorded those which require recording;** you should make copies of your documents and put the originals in a safe place.

This meeting when you sign all the documents should constitute the first meeting of the new trust and like all meetings of the trust, minutes should be taken. You may want to use the sample minutes in Tab 15 of the Trust to get started. At this meeting the Trustees should appoint the Trust Manager and a Secretary/Treasurer. The date of the next meeting should be discussed and scheduled.

Give the Manager/s his/her/their assignments, close the meeting and the Trust is on its way off to a successful start. Now the Manager/s can do all the things required for the Trust as allowed by the Appointment Contract; but, if he/she/they have any problem/s the Trustee/s should be called in to make final decisions, additional contractual appointments, etc.

#### THE OPERATIONS MANUAL:

This manual has several purposes to include helping you better understand the trust articles, assist your management of the trust and instructing you with trust accounting procedures. This manual was never intended to answer all questions that may come up but answer the main ones that arise with every new entity. Again, the manual was not written with specific examples in mind but cover a wide area of the trust matters in general.

#### SETTING UP A BANK ACCOUNT:

Some times some branch managers, and some banks in general (Bank of America and Wells Fargo Bank), don't understand, don't want to understand, or just plain have a discriminatory policy against setting up business trust accounts. This makes it hard for you when the bank does not want to cooperate with you. What do you do in these cases? First, let the bank look over and/or have a copy of your trust indenture if they feel they need it to satisfy their curiosity. Just provide them with the indenture and not the schedules unless they have an absolute need for them. Secondly, they may want the Trustee/s to be on the signature card along with the Manager/s. This should not a problem because Trustee/s do not have to have exclusive check writing privileges. Third, sometimes the bank wants the trust to have a fictitious name or D.B.A. (doing business as) from the county Clerk. This is time

consuming but sometimes faster than fighting them. If you are trying to open the account in a small town where you are not known; the D.B.A. will help. Fourth, never dwell on the fact that the account is for a business trust. Fifth, always be honest. You don't have to reveal everything to be honest, but don't do anything dishonest; it will always come back to bite you.

The Trust is your new form of doing business and making a profit. It can solve a lot of your problems and provide exceptional asset protection and tax savings if properly operated. Treat it like you were running GMC or IBM and your trust business will grow and prosper. You can have the peace of mind that you have done the very best for yourself and your family's future.

Protecting your assets does not happen by accident but losing them does. You have taken the first big step to protect your assets, now you can let them grow inside your trust, protected from your liability, and with the best tax advantages available.

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### **THIRD: INTRODUCTION TO THE TRUST**

Trust law can be very complex to the novice. It is a combination of many different areas of law including principles from the law of property, the law of equity, and the laws of taxation. Most attorneys spend little time studying trusts or estate planning, let alone property, equity or tax law. The IRS states that the majority of our CPAs are inept in certain types of business taxation law, rules, and applications such as partnerships and trusts.

The wealthy go to the most experienced tax and trust specialists who suggest tax techniques that are more effective than the "run of the mill" variety . . . for a very high price I might add.

## EDUCATING YOU ABOUT TRUSTS & TRUST TAXATION IS OUR BUSINESS:

We are not engaged in rendering legal, accounting, or other professional advice or services BUT have carefully studied, analyzed, and identified important ideas in these areas which are useful to the common citizen. It is our intention to present a TRUST MANAGEMENT manual which is designed to inform you about the complexities of trust so you can understand and apply applicable rules and practices to best manage your business enterprise.

### THE PURE EQUITY TRUST:

The type of business trust described in this course, as defined by the IRS, is known as a “PURE EQUITY TRUST” (hereafter referred to as “trust”). In the world of trusts, one can get caught up in a maze of adjectives. “Pure,” “equity,” “revocable,” “irrevocable,” “inter vivos,” “complex,” or “simple.” What do all these terms mean and what are the differences, if any?

*Trusts of this type are commonly referred to as Contractual Business Organizations (CBOs), Irrevocable "Illinois" Land Trusts (ILTs), Unincorporated Business Organizations (UBOs), Business Trust Organizations (BTOs), Common Law Trusts (Colato), Pure [Equity] Trusts, Massachusetts Business Trusts (MBTs), Contractual Companies, or one of many other names or designations.)*

“**Pure**” simply means that the trust is a real trust having a minimum of two Trustees, rather than a partnership, an association or bailment agreement which may sometimes call themselves a trust.

“**Equity**” simply refers to the fact that the trust receives its assets in exchange for units of beneficial interest in the trust rather than by gift or bequest, and that the trust owns its assets in fee simple absolute.

“**Irrevocable**” means the trust that has been declared as irrevocable because the Creator/s, Grantor/s and/or Exchangor/s do not retain any right/s to revoke, amend, or modify the trust or

have the assets returned to them without independent trustee approval.

“**Inter vivos**” because it was set up during the Grantor/s lifetime/s, not after his/her/their death/s.

“**Complex**” because the Trustee/s retain the right to distribute income to the beneficiaries or have the trust pay its own taxes.

The pure equity irrevocable inter vivos complex trust is also sometime called a “Common Law” trust in recognition that it is created under the common law by exercising one’s right to contract and not by any state statute, charter or franchise. Some fairly well known examples of the common law or Pure Equity Trust are the “Massachusetts” and other business trust, “Illinois-type” land trust and other such highly specialized forms as the real estate investment trust (REIT).

The basis for the terminology “common-law trust,” in this connection, is not that this trust is a creature of the common law, as distinguished from equity, but that this business trust is created under the common law of contracts and does not depend upon any statute of the state. [Brown v. Donald](#), (Tex Civ App) 216 SW2d 679; [Colin v. Paine](#), 137 Wash 566, 243 P 2, 247 P 476, 46 ALR 165; [Schumann-Heink v. Folsom](#), 328 Ill 321, 159 NE ALR 485.

The most important requirement to remember at all times is that a “Pure Equity” trust MUST have a minimum of two (2) trustees, one of whom must be independent, who hold their trusteeship in joint tenancy. You can have less than two trustees but then it is considered just a simple or complex unincorporated business organization as opposed to the “pure equity” trust status.

The beneficiaries hold their beneficial interest individually as personal property. Only the trustees may participate in the management of the trust. The beneficiaries cannot participate in the management. If they do, the trust could be treated as a partnership or even as an association. The beneficiaries will have limited liability if they do not



participate in the management. This does not prevent a beneficiary from participating as a trustee however. It is the capacity in which control is exercised which is important. The trust indenture can and does restrict the trustees' personal liability in dealing as trustees.

The trust is a common law entity formed by contract and therefore not subject state regulation as a corporation, not limited to any given state in conducting its business, or does it have any state reporting requirement such as a corporation. It is, however, still required to report its tax obligation and be subject to any regulations covering its particular business operations such as a real estate brokerage, insurance sales, etc. The business trust is an unique package of asset protection strategies and tax savings (not elimination) concepts.

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## **FOURTH: ADVANTAGES OF THE TRUST**

### THE TRUST ARRANGEMENT IN BRIEF:

Your business trust is controlled and managed by designated trustee/s or manager/s appointed by the trustee/s. The trustee/s are generally professionals but members of the Exchangor/s or Grantor/s families and trusted friends are allowed. The trust owns and controls its assets through its trustee/s. All vacancies are filled by the remaining trustee/s or by the Protector if one has been appointed.

The trustees should appoint a chairman from among themselves and a general manager; i.e., someone who has the ability and time to run the trust business on a day-to-day basis.

The activities of the trust are recorded by the Trustee/s in the Trust Minutes which must be consistent with the Declaration of Trust.

The Trustee/s are bound by Resolutions of the Minutes and the indenture. They take an oath of office affirming to maintain them.

The minutes may be subject to amendments, substitution, vacation or restriction as to any such rights.

Your trust may own property in any state or combination of states.

#### WHAT ARE THE ADVANTAGES OF A TRUST:

A trust has many advantages. A trust can reduce taxes or save a person money in other areas by avoiding probate and reducing or eliminating personal liability exposure. The following list suggests some of the things a trust can do:

1. PROTECT FINANCIAL RESOURCES. When property is held in trust, third parties cannot reach the assets unless the asset itself is in question. Individuals can legally declare “I do not own the Property.” This kind of protection is called “insulation from liability.” That simply means a person suing the grantor or the beneficiaries cannot get to the property held in trust if the grantor of the trust does not retain the right or power to revoke the trust.

Easier management of property is another way the trust protects resources. People get old and some become less prudent in their handling of the property. Fewer mistakes are made by putting the property into trust and ensuring that wise and experienced trustees manage it.

2. HANDLE DAILY DETAILS AND ROUTINE. A trust is more efficient than a conventional family operation. The trustees of the trust tend to be more careful in managing the property for they are under a fiduciary obligation to be prudent and careful in the way they manage matters.

3. AVOID SETTLEMENT DELAYS. A trust is a living entity. Successors run it giving the trust flexibility in doing things that a deceased person obviously could not accomplish. The trustees can handle problems that come up. A trust can carry out a wide range of actions in a swift and efficient manner.

For example, when a person dies there is usually a long period of time during which the property is tied up in probate. During this time, it is difficult to sell or lease the property or otherwise use it. With a trust these delays are eliminated. Since the trust owns the property, the trust continues with its daily routine avoiding the delays of probate.

4. REDUCE PROBATE COSTS. It costs a lot of money to go through probate. The major cost is attorney and legal fees. There are attorney's fees on all estates, big and small. Other costs of probate are the filing fees paid to the courts and the "forced sale" of property to pay these fees. When this is necessary, the property usually cannot be sold for its fair market value. What about any costs defending the trust in a court suit situation. Often, when a person dies an heir may say the last will and testament was fraudulent, etc. If the fight is prolonged, the only ones to profit are the attorneys. Appraiser and guardian fees also deplete the estate.

While trusts have administration costs, they can be minimized by selecting people who will work for nothing or a low fee. Close friends or family members oftentimes serve as successor trustees and do not request any administration fees.

5. REDUCTION OF TAXES. One of the most useful advantages of a trust is the reduction, or in some instances complete elimination, of income and/or estate taxes. When a trust is properly constructed it provides "income splitting" advantages. That is, money (*passive and portfolio income*) earned by the trust is separated from money that is earned by the person who gave the property to the trust. For example, a taxpayer earned \$30,000 from their job, and another \$25,000 from passive income making them pay taxes on \$55,000. When they put the passive income into a trust, the trust could pay taxes on the \$25,000 and the taxpayer would move into a lower tax bracket. Dropping from the higher tax bracket to the lower bracket offers a tremendous savings.

The use of a business trust can eliminate self-employment tax provided the worker receives income as a W-2 wage earner. Trusts, in general, are allowed to donate up to 100% of their income to bonafide charities which is another way to lower the tax liability.

Estate tax (*that is the tax paid by the estate when it exceeds the "lifetime exemption"*) can be transferred to their heirs. These taxes can be avoided by placing property in an irrevocable trust. Since an irrevocable trust does not expire when the person dies; there is no estate to be taxed or probated provided all the requirements have been met.

6. PROTECTS PRIVACY. A trust does not have to be registered as opposed to a corporation (*except in Nevada; see Nevada Revised Statutes, Chapter 88A - Business Trusts*).

A corporation must file a report every year revealing the officers of the corporation and paying renewal fees; the business trust does not. The business trust must file a tax return each year but it has considerably more privacy than other forms of business organization. The trust instrument does not have to be filed in a public place as do corporations while the trust can accomplish the desires of the Creator/s without making it public. The most prudent people in the country have trusts which serve this purpose and you might want this same type of privacy for your affairs.

7. ASSURES SAFER AND IMMEDIATE DISTRIBUTION. The nature of a trust is such that the trustees must follow the instructions as outlined in the trust indenture. Your wishes are carried out as stated and monies can be easily distributed for the management of the trust and/or trust property plus distribution to the beneficiaries.

8. PROVIDES FLEXIBILITY. A trust is one of the most flexible forms of organization imaginable. It can engage quickly into any legal transaction such as buying, selling, leasing or

otherwise dealing with its property. This type of flexibility and control is very valuable because emergencies and other immediate needs can be solved on the spot. A trust can provide desirable results for a possible divorce, needy children, aged parents, carrying on of a business after the death of the major owner, management of property in an efficient manner, and any number of other things as specified in the trust indenture. It is very important not to limit the usefulness of the trust in its indenture.

9. OPPORTUNITIES FOR CHARITABLE GIVING. A trust can donate up to 100% of its adjusted gross income (AGI) to charity. As an individual you are restricted to a maximum of 50% of your AGI to a public charity while the corporation can contribute only 10% of its AGI.

OTHER PURPOSES SERVED BY THESE TYPES OF TRUST:

1. Forming an organization so there is little or no liability against the members.
2. Avoiding the payment of additional taxes and fees as are required of corporations.
3. Avoiding the filing of detailed periodic reports of operation and financial conditions that corporations must file.
4. Securing of capital by the sale of “shares” without the need to comply with various state statutes.
5. Doing business in other states without going through a lot of “red tape” and regulations.

In conclusion, a business trust can save you money, lower (but not eliminate) tax obligations, avoid probate or unnecessary attorney fees and delays, manage your family and business affairs more efficiently, protect your loved ones from others, protect your property, maintain better records, protect your privacy and accomplish many of your desires, both now and after your death, in a most efficient manner.

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## **FIFTH: THE BUSINESS TRUST**

Naturally, to accomplish all, or even a large number of these goals; the trust must be carefully created. No simple trust could do all this. Only a complex trust carefully drafted and properly administered can. Our purpose is to teach you how to use your trust to give you these advantages.

### WHAT IS A TRUST?

A trust is a special type of legal relationship. Black's Law Dictionary defines a trust as a "right of property . . . held by one party for the benefit of another."

Most importantly, a trust is a confidence that one person (called the grantor) places in another person (called a trustee) for the benefit of a third person (called a beneficiary) with respect to property the trustee holds for the benefit of the beneficiary. This is the typical P-A-T or principal, agent, and third party arrangement.

It is for this reason that a "fiduciary relationship" exists because the trustee owes fiduciary duties to the beneficiary. A fiduciary (a trustee) is one who is in a special position of trust, confidence, or responsibility, to do things for others (the beneficiaries).

A trust is created when a person decides to create a trust. As Grantor, he/she draw up a trust indenture, or a declaration of trust, which sets forth the desires as to what the trust will do and who will benefit. The trust documents will identify who will be the trustees to manage the trust. After the trust is drawn up the grantor gives the property to the trustee to hold. The property is called the trust corpus. The trust is then in existence and begins to operate.

### TRUST AGREEMENT:

The trust agreement is the "constitution of the trust." As already mentioned above, the trust agreement is frequently referred to as the

“Trust Indenture” or “Declaration of Trust”. You should familiarize yourself with its contents and carefully stay within its guidelines.

#### KEY PERSONS INVOLVED WITH A TRUST:

There are four key people, or groups of persons, who deal with a trust.

1. GRANTOR -- the person, or persons, who set up the trust. This person is also called the creator, exchangor, trustor, or settler.
2. TRUSTEE -- the person or persons who run the trust.
3. BENEFICIARY-- the person, or persons, who receive the benefits from the trust. They hold Units of Beneficial Interest or UBI's.
4. THIRD PARTIES --- any outsider dealing with the trust.

**NOTE:** Person is further described as “*an individual, corporation, business trust, estate, trust, partnership, joint venture, government, governmental subdivision, agency, or instrumentality, or any other legal or commercial entity*”.

#### THE GRANTOR:

The grantor is the person (or persons) who creates the trust. The grantor decides that a trust is what he/she/they want and so takes the necessary steps to establish the trust. The grantor may also act as a trustee of the trust (this must be done very carefully). However, to avoid adverse tax consequences, if a grantor/s is/are going to be a trustee, he/she/they should not be the initial trustee but should be voted in later. The grantor/s could also be a beneficiary.

If a grantor were to occupy all three positions at the same time and did not have an independent trustee acting at the same time; the trust would be useless and therefore destroyed because of illegal acts.

### TRUSTEES:

The trustee is the person, or persons, who receives property from the grantor. They operate, control, and have power over the trust. The trustee is the person who holds LEGAL TITLE to the property for the benefit of the beneficiaries. After the grantor/s transfers his property to the trustees, the grantor/s does not own the property any more. Technically, the trustees then become the owner of the property but are very limited as to the use of the property.

Any person old enough to manage their own affairs, as long as they are an adult and mentally competent, can be a trustee. A corporation may be a trustee as long as the articles of incorporation allow it to hold trust property. A foreign person or corporation can be a trustee. Also, another trust can be a trustee.

### BENEFICIARY:

The beneficiary of a trust is the person for whose benefit the property is held in trust. The beneficiary holds the EQUITABLE TITLE to the property held in trust. It is not a real “title” that the beneficiary could look up in a public office, but it is a right the beneficiary has which a court will protect. The beneficiary is the one who gets the advantages or profits from the existence of a trust.

The grantor has the right to decide who will be the beneficiary(ies) of their trust. To avoid a gift tax, the grantor should be the first beneficiary of any trust.

The identity of the beneficiaries of the trust must be clearly defined. They must be listed by name, address, or by some other means so that a “reasonable man” would be able to identify them without much difficulty. That does not mean the beneficiaries must be named in the trust per se but some form of intention or identification must be available to the trustee/s.

### UNITS OF BENEFICIAL INTEREST:

Units of Beneficial Interest (UBIs) are merely the rights to enjoy the monetary profits, or other physical benefits, resulting from a trust,



contract, estate, or property rather than the legal ownership of these things; thus providing a more flexible way for the identification of the beneficiaries. UBIs are transferable within unique restrictions and exceptions. Therefore, the "beneficial interest" of the trust can be easily shifted from one person to another without excessive complexity. Initial UBI holders, along with the number of units they own, are recorded within the trust UBI Registry. Beneficiaries may then transfer all, or some, of their Units simply by filling out the reverse side of their "evidencing certificate" and surrendering the Certificates to the Trustee for re-issue. More precise procedures are outlined within the Agreement.

#### THIRD PARTIES:

This is a phrase to describe anyone other than the grantor, trustee or beneficiary who deals with the trust. The term "third party" generally means anyone who is outside of the trust. Actually, it would include anyone who tries to deal with, sell to or get something from the trustees because of the trust.

#### THE TRUST AS A SEPARATE ENTITY:

A trust is treated as a separate entity for tax purposes. All money earned by the trust is taxed to the trust unless it is distributed to beneficiaries and then at their tax percentage. The tax deductions taken by the trust can only benefit the trust, no one else. The single most important advantage of creating a separate entity for tax purposes is to achieve income splitting.

A trust is treated as a separate entity for liability purposes in most states. When a trust enters into a contract with someone and the trust breeches the contract, the only person that can be sued is the trust, not the officers, trustees or beneficiaries. The only property or money the suing party can get is the property held in the name of the trust, this is called "Limited Liability". When the grantor places property in trust irrevocable; the property is beyond the reach of creditors.

### GIFT TAX CONSIDERATIONS:

1. The creation of common-law trusts were held lawful and subscription to stock (units of beneficial interest) in a common-law trust was ruled as an investment, not a gift. [Palmer et. al. v. Taylor et. al., 269 S. W. 996 (1925)]
2. Gift tax applies only to transfers by gift with less than full and adequate consideration. [Tyson v. Commissioner, 146 F 2d 50 (1944)]
3. Even bad bargains in a genuine transaction do not result in taxable gifts. Where the value of stock (UBI) was in excess of the consideration, the transfers were made in the ordinary course of business and were not subject to gift tax. (Leon Jaworski argued this case against the IRS.) [Est. of Anderson, 8 T. C. 706 (A) (1947)]
4. No gift tax applies when property transfers to a disconnected and isolated entity where consideration is not lacking. [Scanlon v. Commissioner, 42, U.S. Board of Tax Appeals 997 (1940)]

### THE IMPORTANCE OF STATE LAW:

The laws that determine how a trust is created, administered and how people are to act with respect to the trust are established by the legislature and courts of each state. The law of trusts is very similar throughout the United States. These laws are based upon the Common Law of England. Although Federal law determines the tests for taxing trusts, state law determines what the property rights or interests are in order to apply those taxation tests.

### FOUR ELEMENTS NEEDED TO CREATE A TRUST:

Under state laws there are four major requirements for the creation of a valid trust. They are as follows:

1. INTENT TO CREATE A TRUST. There must be an expressed intent by the grantor indicating he/she desires or purposes that a trust be created.
2. SPECIFIC DESCRIPTION OF PROPERTY. There must be a specific description of the property that the grantor is transferring into trust to the trustees. Land should be by legal description and personal property should be described so it can be easily identified.
3. NAME OF THE TRUSTEES. The names of the initial trustees must be identified. Other trustees may be added or removed later.
4. NAME OF THE BENEFICIARIES. The names of the beneficiaries must be ascertainable by a third party (on a need to know basis) as indicated on schedule "C" of the trust.

#### CONSIDERATION:

No consideration is necessary for the creation of a trust. It is clearly the law throughout the United States that the grantor can establish a trust without receiving any payment of any type. The UBI's the grantor/s receive/s is/are of equal value to the assets put into the trust.

#### DESCRIBING A TRUST:

The trust may be described by any characteristic it possesses. It may be described by the time when it was formed or classified as to the location of operation. A trust may be categorized by the complexity of its operation (for examples, simple, complex, multiple or layered). A trust may be categorized by the person for whom it is intended to benefit (such as grantor, non-grantor, support, educational, split interest, spendthrift, sprinkling, shifting, annuity, marital, common trust fund, honorary, charitable etc). It may be described by its permanency (revocable, irrevocable). The trust may be described by the type of property to be found in it. There is no special rule that says a trust must only be described by one phrase. The overall name we have

given the type of trust described herein is a “PURE EQUITY TRUST.”

#### MANAGING THE TRUST:

At this point, you, the grantor(s) and your trustees, are looking for some guidance in running, administering or managing the trust. This manual provides some general guidelines for the operation of a trust. These guidelines are divided into major headings. These particular headings were selected because they cover most of the common operations you will encounter. They are set forth to instruct you in handling certain situations should they arise. These are only suggestions; you do not have to follow them. In fact, based upon your own outside reading, you may decide to do things quite differently.

Trustees always have questions. If you need advice about the operation of your trust, we suggest you join an organization which specializes in providing a cooperative pool of information and assistance for trustees. This organization should be made up of trust specialists and trustees like yourself who work together and share information about the most effective ways to manage, administer and operate a trust. By joining this type of organization and paying any necessary fee charged for their service you can avail yourself of the advice, counsel and wisdom of the organization and the staff it provides.

#### READ THE TRUST INDENTURE:

The most important guide you will ever have in running or operating the trust is the trust indenture. It determines who can do what, how, where and when. If the trust indenture states a certain action can be taken, then it is all right to do so. If the trust states a certain action cannot be taken, then it is forbidden. If the trust indenture states a certain type of action must be carried on in a certain manner, then you and the other trustees must take that action in that manner. You cannot do it differently. Many of the questions you may have about running the trust will be answered within the trust indenture.

### HOLD MEETINGS OF THE TRUST:

The trustees of a trust must hold meetings to decide what to do for the trust. Those meetings are part of the trust operation and any expenses incurred in holding trust meetings may be tax deductible by the trust. Therefore, whenever you hold a meeting, be sure to indicate those expenses made by the trust in connection with that meeting.

Meetings of the trustees can be held at any time and any place upon notice to the other trustees. Meetings must be held at least once each year in order to make any important decisions or take any important actions with respect to the trust. This meeting is to be held 30 days before or after the end of the calendar year.

A meeting is called by notifying the trustees. There are three ways to give notice of a meeting to the trustees:

1. Personally telling the trustees of the meeting,
2. Sending a letter to the trustees, or
3. By telephone.

Notice of a meeting must be given before the meeting begins. There is no time limit as to advance notice. Only trustees may call a meeting.

Not all trustees have power to approve all actions. The grantor, for example, as trustee does not have power to approve any distribution to himself. Nevertheless, the grantor as trustee, may be present at the meeting.

One of the most useful methods for holding a meeting is by telephone. All trustees are deemed present at the meeting when on a conference call. A telephone conference can be arranged by asking the operator.

As we shall point out under the heading of "Protecting Trust Privacy," permission to release any of the information or records of the trust can be given only at a Board of Trustees meeting. No such permission can

be given by any individual trustee. This is to protect the privacy of the trust.

#### MINUTES:

Whenever trustees hold a meeting they should keep a record of their decisions. This record is known as “minutes” of the trust meeting. There are no special forms needed for the keeping of minutes. A person should be chosen to take the minutes of the meeting. That person might be called the acting secretary of the trust. Whenever a decision is made it should be written down. At the end of the meeting those decisions are typed up and signed by the secretary and then filed in the trust books. This will become a permanent piece of documentary evidence to prove the actions taken by the trustees were, in fact, approved formally and officially by the board of trustees. THIS IS VERY IMPORTANT.

Whenever the trustees disagree in any manner with regard to the approval of the action, this should be recorded in the minutes. This may be of assistance in later proving the trustees were acting in an adverse relationship. If the independent trustee makes such comments the other trustees should not be offended.

Sample of minutes are included at the end of this handbook.

#### ADVERSE TRUSTEE RELATIONSHIP:

This is another very important trustee position. If the actions by the trustees are not approved by an adverse trustee, there is a risk the trust will be considered a “grantor type trust” and be taxable to the grantor or creator. Therefore, it is important that the trust have an adverse trustee.

Who is this adverse person? This is one that owns some units of beneficial interest in the trust and who would be adversely affected by the exercise, or non-exercise, of a power which they possess in respect to the trust. It cannot be the grantor. Children of legal age that own UBI’s could be adverse trustees. If your children are very young and

own UBI's, and you have appointed a guardian for them, that person could be in an adverse position.

#### THE INDEPENDENT TRUSTEE:

The independent trustee is really not a person but a situation where no more than fifty (50%) percent of the board of trustees are related to the grantors by blood, marriage, adoption, or employment. The independent trustee, like the adverse trustee, is also good for tax purposes. When decisions are made by an independent trustee the IRS looks at the trust as a non-grantor trust, and this has very good tax advantages.

#### RECORDING CERTIFICATES OF BENEFICIAL INTEREST:

When a trust uses certificates of beneficial interest, it is important that changes in beneficiaries be recorded on Schedule "C" Continuation of the trust and signed by the trustees. The trust can use certificates, just the Schedule "C" Continuation, or both; but the beneficiaries must be notified of their position.

The trust indenture requires the beneficiaries to be ascertainable. By having an up-to-date record of the names of all holders of UBI's and the number of units each holds; this requirement will be satisfied.

Whenever UBI's are given to a child, it is best for the person on the back of the certificate to say: "I hereby give (so many) units of beneficial interest to Johnnie Jones, delivering the same to his guardian, Mary Jones." It is arguable that parents could designate another adult, other than themselves, to act as the "guardian" of their children. We recommend this guardian be someone other than the grantor, or the grantor's spouse.

#### RECORDING THE NAMES OF THE TRUSTEES:

The trust indenture requires all trustees to sign acceptance papers when they become trustees. These are attached to the trust indenture and made a part thereof. Trustees may resign at any time, or be removed from the trust. In order for outsiders and third parties to rely upon the authority of the trustees to take action on behalf of the trust, there must

be some method to record the names of the present or current trustees. The best way to do this is to record it on an acceptance form. When a trustee resigns they must resign in writing and have the paper notarized. Then they should sign “correctory” deeds to all real property over to the new trustee/s as trustee/s to keep the title clear and make transferring title later much easier.

#### ADDING AND REMOVING TRUSTEES:

Any adult can be added as a trustee, as long as the other trustees agree. The form to use for this is entitled, “Acceptance of the Trust.” Adding or removing a trustee must be at a trustee’s meeting and a record must be kept.

If a trustee wants to resign, he needs to submit his notarized letter of resignation to one of the other trustees. This action should be noted in the minutes of the next meeting of the trustees.

A trustee can be removed from office only when they have done something wrong and only when the other trustees unanimously agree to remove them. When the independent trustee resigns or is removed, the new trustee must also be independent.

#### THE PROTECTOR:

The use of the protector is not used much in America but internationally is used. The protector is appointed by the grantor and has only the power to hire and fire trustees. This should only be done for cause, and if the trustees are not following the trust indenture. But nevertheless, the protector has the power to fire trustees.

#### KEEPING THE TRUST PROPERTY SEPARATED:

The money which belongs to the grantors, trustees or beneficiaries as individuals should never be mingled with money belonging to the trust. Likewise, if the trustees are depositing money which has been earned by, or belongs to, the trust, they should not deposit that money in a personal bank account. The trustees should set up a bank checking account entitled “ABC Trust,” or whatever the trust’s name. Remember, as an individual you can do anything you want to with your



own money. When you are working with trust money, however, you must be more prudent.

Real property belonging to the trust should be transferred into the trust name with the trustees holding title as joint tenancy on the deed. This could be done with a contract of sale but should be done with a deed, recorded with the county clerk. Personal property should be inventoried and some type of earmark or label should be attached to it.

When trustees keep trust property separate from their own, this is evidence that a real trust exists. This is important for tax and other legal purposes.

#### TRUST ASSETS:

The trust assets are the “corpus” of the trust as well as the retained earnings therefrom. The corpus generally consists of the assets the grantor transferred into the trust at the time of its creation. These are the assets that the trustees must administer for the benefit of the beneficiaries.

#### PROTECTING TRUST PRIVACY:

A trust is private. It is designed to be private. To insure that privacy, the trustees must not release information about the trust, or the trust records, to anyone without the express, unanimous approval of all the trustees, in accordance with the trust indenture. When there is delay in holding a regular meeting of the trustees, there is delay in giving permission for the release of information. That cannot be avoided, however, because this is a very important part of the trust and cannot be violated by the trustees.

Should a bank, title company, or any other third party ask a trustee to expose the records of the trust; the first thing the trustee should say is:

“I’m sorry the records are confidential. If you will be kind enough to submit a request in writing, it will be brought before the board of trustees for approval at the next regular meeting. No records

can be released from the trust without the approval of the board of trustees.”

If you are dealing with any government agency, it is best to say nothing. Instead, politely indicate that you will talk to your attorney and will get back to them. Say nothing more. In your haste to cooperate, you may say something that is not entirely accurate which could be used against you in a court of law. The law is VERY COMPLICATED and you should not try to explain anything to a government agency without the assistance of an attorney. It is always best to allow your attorney and/or accountant to review the records and act on your behalf with the government agency so all information can be presented in a clear and precise manner that is most advantageous for you under the law. The trust indenture obligates you not to release any information without the approval of all of the trustees.

Notice is hereby given to all persons, companies, or corporations extending credit to, contracting with, or having claims against the Trust, or the Trustees thereof, that they must look only to the funds and property of the Trust for payment, or settlement, of any debts, tort, damage, order, judgement or decree, or any indebtedness which may become payable hereunder; that the Trustees, officers, or agents are mere Independent contractors, and not personally liable when dealing with the Trust properties, or matters. <sup>1</sup>

#### DISTRIBUTION TO BENEFICIARIES:

A distribution to a beneficiary is the transfer of corpus or income from the trust to the beneficiary. Nothing goes from the trust or the trust bank account to a beneficiary without a formal action by the trustees approving such “distribution.” If money is paid out for expenses, they

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<sup>1</sup> To insure protection to the Trustee(s), this “Notice” MUST be affixed, by exhibit, inked stamp, or hand written statement, to every contract signed by the Trustees. See [Betts v. Hackathorn](#), 159 Ark 621, 252 SW 602, 31 ALR 847; [Henry G. Taussig Co. v. Poindexter](#), 224 Mo App 580, 30 SW2d 635; [Byrnes v. Chase Nat'l Bank](#), 225 App Div 102, 232 NYS 224 affd 251 NY 551, 168 NE 423; [Rhode Island Hospital Trust Co. v. Copeland](#), 39 RI 193, 98 A 273.

must be expenses related to the operation of the trust. They cannot be expenses for the personal enjoyment or personal necessities of the trustees. All money is to be used for trust business and/or the benefit of the beneficiaries. All distributions must be approved by the trustees before being made.

Distribution **must be made** in accordance with the ascertainable standards. That is, if the trust indenture provides that distributions must be made for the, “care, maintenance, extra-ordinary educational needs, medical expenses or emergencies of the beneficiaries;” those are “ascertainable standards.”

When the board of trustees meets to make a decision to distribute money to one of the categories they should write in the minutes that a distribution was made accordingly.

When money is actually distributed for the use of the beneficiary, a record of that payment must be placed in the books as a distribution to beneficiaries. The beneficiary will be taxed upon that as income.

**NOTE:** Beneficiaries receiving income from the trust during the year must pay estimated tax on the money they receive. If more money is paid out; the beneficiary may be involved in a “throw back rule.” If this is your situation, please contact your trust representative or someone who understands that rule. While income splitting advantages are still retained, the “throw back rules” eliminate the advantage of deciding during which particular year and under which particular conditions tax benefits will be granted by using a trust.

#### INSURANCE AND THE TRUST:

Ordinarily, the insured owns their life insurance policies. That means, the policy is in his/her name and he/she is called the “policy owner.” One of the biggest estate tax advantages is to get the ownership of the life insurance policy out of his/her name and into the name of the trust. This is not a difficult task. The owner merely contacts the issuing insurance company indicating that he/she wants to transfer the policy

ownership into the name of the trust. In transferring a life insurance policy into the trust, it is important the premiums be paid by the trust, not by the insured. Payments for fire, auto or the like types of insurance are ordinary and necessary expenses of the trust if they are to protect and preserve the property of the trust.

#### SALE, EXCHANGE & DEALINGS WITH TRUST PROPERTY:

The trustees have broad powers to deal with the property of the trust. They may sell, exchange, rent, and do any one of a number of things with respect to the trust provided such actions are taken carefully and with forethought. The trustees do not really own the property . . . they are merely using it for the benefit of the beneficiaries.

No piece of property owned by the trust should be sold, exchanged, leased, or otherwise handled without the approval of the board of trustees in accordance with the terms of the trust indenture.

It is always a good sound business practice to write all important decision into trust minutes. This serves the purpose of proving the trustees are acting in their capacity as trustees and also constitutes a written memorandum which will prove the terms of the arrangement are being adhered to.

#### HIRING AND PAYING CARETAKERS:

Only the trustees can hire a manager or caretaker. The trustees should place a simple advertisement in a local paper in the city or county where the land is located. If the trustees want, they may post that advertisement in other places throughout the community such as on the county bulletin board, the supermarket bulletin board or elsewhere.

#### PAYING TRUSTEE AND CONSULTING FEES:

The trustees are entitled to be paid reasonable compensation for the work they do on behalf of the trust. Naturally, they cannot be paid twice for the same thing. If any trustee acts as a caretaker of the trust property, and is paid for that service, they cannot be paid also as a trustee for doing the same service. Trustees can be compensated for attending official meetings of the board of trustees. Compensation can

be for a given amount of money per hour, or for a given amount of money for each meeting plus out of pocket expenses. Neither trustees nor caretakers should wait long periods of time without being reimbursed for their expenses.

#### BORROWING FROM THE TRUST:

If any money is loaned to someone from the trust, it must be done in writing and done carefully. This is especially true when money is loaned to the grantor/s. The most important requirement is that such a loan be approved by the complete board of trustees and the loan agreement should include adequate interest, adequate security, and a pay back plan.

#### WHAT TO DO IF THE TRUST IS SUED:

A trustee assumes no personal liability as long as the exercise of their power is within the terms of the trust indenture. The first thing that should be done in the event of a lawsuit is to contact your attorney. Do not give any statements or write any letters concerning the matter until you have had an opportunity to discuss the matter with your attorney.

#### TERMINATING THE TRUST:

The trust is irrevocable but it can be terminated with the consent of the board of trustees and the approval of all the beneficiaries of the trust. This should be done in writing on a form which specifically provides all the beneficiaries are acting together. Have all beneficiaries sign the document in front of a notary public and place this document into the trust records. Terminating the trust is such an important action that it is best to consult your attorney or trust agent before you do this. They will evaluate the situation and explain any or all tax consequences.

#### PAYING EXPENSES OF THE TRUST:

Only money spent which is specifically and actually connected with the operation, management, or running of the trust can be an expense of the trust. Whenever possible, expenses of the trust should be paid by check from the trust checking account. This will be a useful record and prove the operations of the trust to be separate from those of the

individuals acting as its trustees. Expenses incurred in the administration, management, conservation and protecting of the trust are:

1. Reasonable compensation of the caretakers and trustees for work performed on behalf of the trust.
2. Reasonable compensation for any person or entity which provide service, articles or utilities to the trust or on behalf of the trust property.
3. Any expenses in the operation, maintenance, cleaning, repair or otherwise caring for the property of the trust.
4. Any expenses in providing necessary supplies, equipment, and materials on behalf of the trust either by means of purchase, lease, rental or otherwise.
5. The payment of taxes, charges, assessments or license fees on behalf of the trust or the trust property.
6. Expenses of capital improvements on behalf of the trust property.
7. Insurance premiums with respect to policies owned by the trust and of which the trust is the beneficiary.
8. Any legal fees, bookkeeping fees, accounting fees, tax advisory fees or other professional expenses on behalf of the trust or incurred for the purpose of running the trust.
9. All other ordinary and necessary expenses incurred to care for the trust and its property.

These categories are broken down later in the workbook.

### DEALING WITH MINORS AS BENEFICIARY:

A minor is a person under the legal age. In most states this is twenty-one (21) years of age but many states have lowered it to eighteen (18) years of age. Persons under that age do not have legal capacity and may not enter into contracts or take any actions which will have binding legal results on their behalf. For this reason, extreme care should be exercised in dealing with minors who are beneficiaries of the trust. We suggest a guardian of such minors be appointed other than the grantor or the grantor's spouse.

### DEALING WITH THE INTERNAL REVENUE SERVICE:

First, there is one all-important piece of advice for people to remember when dealing with the Internal Revenue Service ( IRS) . . . DON'T. When approached, contacted, or receiving any written communication from the IRS requesting information, or stating notice of audit; etc., do not speak with them directly. This is not given for the purpose of encouraging you to be discourteous to members of the IRS. The purpose of this advice is to keep you from releasing any information whatsoever to the IRS that might come back to injure you or cause the trust unnecessary problems.

**NOTE:** The Courts have ruled that "A citizen is under no obligation to do any particular thing. A citizens failure to act creates no liability, but if a citizen voluntarily attempts to act and do the particular thing the citizen comes under implied obligation in respect to the manner in which the citizen does it." Waivers of Constitutionally protected rights not only must be voluntary, but must be knowingly intelligent acts done with sufficient awareness of relevant circumstances and consequences. (See [\*Gardian T & D Co. v Fisher\*](#), 26 S.C.T. 186 at 188; [\*Brady v U.S.\*](#), 397 U.S. 742 at 748)

If, or when, contacted by the IRS say, "Whatever you want, put it in writing, and I will refer this matter to my attorney." If you say more than this you have said too much. Some people believe if they cooperate with an agent of the IRS, it will be better for them. This is not true! They do not bend rules or grant privileges or favors to

people who cooperate. Just because their last name is "Service" doesn't mean they are here to serve you - the taxpayer.

Secondly, the IRS could be classified as one of the most powerful organizations in the U.S. Considering that the IRS is solely responsible for collecting Federal taxes and imposing penalties for late, understated, or evasive filings, the IRS poses one of the largest financial threats to many individuals and business owners. To sum it up, the IRS has unique information resources, legal standing, and roles as a law enforcement agency. On top of that, the IRS also acts as a legislative-originating authority with a large amount of freedom to make mistakes with out consequences (no one can penalize the IRS for incorrect tax accusations).

So what can we do to minimize the IRS's over-inflated accumulation of power and protect ourselves from its potential for financial wrath? Unfortunately, if there were a concrete answer for that, the IRS wouldn't be the intimidating and widely feared agency it is today.

Since the IRS uses what filers provide (along with other miscellaneous resources) to help determine the accuracy of accused filings, our defense is greatly reduced. That's the IRS's whole idea! There is one thing we can do, each day, to better prepare ourselves for possible tax evasion accusations . . . keep records.

Quite possibly, our best defense against audits and false evasion accusations is to keep accurate, detailed records of cash flow, payments, earnings and other financial motions. Depending on your profession and your position within it, your specific approach could be extensive and time consuming.

A meeting with your financial advisor or accountant is a great place to start to find advice on what financial records and statements are the best to focus on to keep up your guard. Generally speaking, the greater volume of records you keep (and their accuracy), the better your chances are for surviving an all-out IRS battle.



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## **SIXTH: BUSINESS TRUST BOOKKEEPING**

### TRUST BOOKKEEPING:

An old adage says “knowledge is power” but with trusts it should read “information is important.” If people do not know what they have done with their money or property they can be taken advantage of. Another proverb says “You can’t tell the players without a program.” Likewise this is true with trusts as in all other affairs in life. You can’t prove what you have done without a record of the act.

As you know, it is very important to be careful with your own things and it is more important to be careful with respect to those things that belong to others. Since a fiduciary is taking care of property for the benefit of others (the beneficiaries); they have an important duty to take care of the things which are not their outright but in their care for the benefit of others. One of the trustees’ specific duties is to keep accurate records of the trust income and expenses, asset acquisition and disposition.

Another important reason for keeping good records is to prove the trust’s income and expenses for tax purposes. The only way you can prove an expense is to keep good records. If you want your trust to be able to take all of the deductions allowed by law you must maintain proper records so your accountant can prove the deductions to which you are entitled. As with most people, you will want to save every dollar possible. That means you must learn some simple steps in keeping books.

### KEEP IT SUPER SIMPLE:

The trustee spending the money must make some simple bookkeeping entries which will make it possible for the accountant to do the rest of the work. As long as that is necessary, it should be as simple as possible.

If you remember only two simple rules in keeping your records, you will never have any major troubles in record keeping. They are:

1. DO IT NOW . . . NOT LATER, and
2. WRITE DOWN EXACTLY WHAT IT WAS FOR.

When money comes into or you pay any money out of the trust, write it down right at the time. Do not wait for an hour, a day or a week to pass before writing down what you spent. Do not write a check and try to figure out later who the check was written to. If you write down what the expense was at the very moment you paid it you will never have to worry about forgetting. Even if you forget, the written record can be used by the accountant to prove what it was for. If you spent cash out of pocket to buy something for the trust, ask for a receipt. On the back of the receipt write down what it was for.

In conclusion, these two simple points are the most important of all: (1) write it down at the time you spent it and (2) describe exactly what the payment was for. If you learn nothing else from this booklet, remember these two simple rules.

Bookkeeping forms are not something you need to buy if you want to make your own. There are samples in your trust portfolio.

#### MONEY COMES INTO THE TRUST (INCOME):

When any money comes into the trust, it is called income. When any money goes out of the trust, that is called expenses. There are few exceptions. To make sure there is no mistake, always write down each item of income and each payment that goes out, whether it is check or cash. When any money or anything of value comes into the trust, write it down on the "Trust Income Sheet." That is the sheet where all income is entered. If you do not write it down, odds are you will forget about it, lose it, or write it down incorrectly somewhere else.

A standard rule in trust record keeping is to do everything by check. Deposit the full amount you received in the checking account. Do not

withhold any cash whatsoever. This way there would always be a record of the full amount of all deposits in your checkbook. There would always be a correct record of all money that went out of the checking account because of the record of each check. This could avoid problems later on when the accountant is trying to determine the taxes.

Let us go over it one more time. First, write down on the “Trust Income Sheet” the full amount of all money you receive, then deposit the full amount in the trust account. Don’t take anything out when you make the deposit. If you need cash for petty cash, write yourself a check so there is a record in check form of what you did.

Don’t worry about the bookkeeping category column. We are not concerned if you are sophisticated and knowledgeable in using that column. If you cannot write down what you took in and what you paid out, you cannot expect the accountants to have an adequate bookkeeping system.

#### CATEGORIZING THE TYPE OF INCOME:

We are now going to point out a few simple explanations for deciding which bookkeeping category to use concerning trust income.

##### BUSINESS INCOME:

Business income is income generated by business activity. A business is a special activity, other than your employment, which is set up to earn a profit (even if it takes a loss). For example, a business can be a farm, pigeon sales, artistic, a print shop, delivery service, multi-level marketing, or any other specific and identifiable operation.

If you are an employee somewhere, that income (W-2 reportable) CANNOT go into the trust as income. If you wish to put it into the trust you must first pay the taxes and then put it into the trust as a capital investment, loan, or gift. Don’t think of it as a business. A business would be a special and separate operation, no matter how small. Remember, there is no such thing as a part-time business.

Some people have more than one business. For example, a person could have a janitorial service, and be engaged in multi level sales at the same time. These types of income would go on the trust income sheet as business income.

DIVIDENDS:

A dividend is money you receive because you own stock in a corporation. When you receive this type of income you put down dividend income on the trust income sheet.

INTEREST:

Interest income is money that you earn as interest on your saving account or on money which you have loaned to someone. Do not confuse interest received with principle received. If you receive any money from the bank as interest or any other interest from anyone for property or money you have loaned, enter it on the Trust Income Sheet as interest income.

PRINCIPAL:

When the trust sells an asset, some or most of what the trust receives could be principal and not income. The trust should keep a ledger on what is principal so the trustees can determine what is income and what is principal.

PARTNERSHIP INCOME:

Partnership income is income received from a partnership. A partnership is one type of business entity. That is to say, a business could be set up under four different methods: (1) a corporation, (2) a partnership, (3) a business trust, or (4) a sole proprietorship. It is not advisable for the trust to be a general partner. If it were, all the assets of the trust could be vulnerable to the liabilities of the partnership. If the trust were a limited partner, this would be acceptable as there can be no run over of liabilities from the partnership.

### RENTAL INCOME:

You may own property that you rent. The trust may own an apartments or houses for rent. Any income you receive from the tenant is rental income. You would record this on the Trust Income Sheet as rental income.

### SALE OF A CAPITAL ASSET:

A capital asset in broad terms is anything acquired by the taxpayer for personal and investment purposes. For example, a house, a piece of land, special equipment, gold or silver would be considered to be capital assets. This would also include property that the grantor placed in trust as corpus. The money you receive whenever you sell a capital asset is called capital gain. You would record this on the Trust Income Sheet as a sale of a capital asset. This may or may not be taxable, see your accountant.

### MISCELLANEOUS:

The phrase "Misc." means miscellaneous income. Anytime you receive income which does not fall into one of the above categories, call it Misc. For example, if you borrowed money, a gift, or anything else you might get money from.

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## **SEVENTH: BUSINESS TRUST EXPENSES**

### MONEY GOING OUT OF THE TRUST (EXPENSE):

There are two grand divisions of expenses. One is called "*ordinary expense*" and the other is called "*capital expense*". The type of expense you will most often incur is ordinary expense. It involves spending money to build something that is intended to last a long time, or purchase something that will last a long time.

#### 1. CAPITAL EXPENSE:

The following are the most common examples of *capital expenses*: (1) buying a house, (2) purchasing furniture or any equipment and (3) making improvements to a house, building

or land. They are called *capital expense* because they are used to add to, or improve something that is going to last for a long time as an investment.

**NOTE:** When you pay for land in installments, list this under an *ordinary expense* category known as installment payments.

## 2. ORDINARY EXPENSES:

The most common expense you will have during the year will be *ordinary expenses*. There are only about twenty-five categories with which you need to be concerned. Remember, you must write down all of the information you can on the Trust Expenses Sheet each time you have an expense.

If you are not able to figure out the bookkeeping category, at least be sure to enter the other information on the Trust Expense Sheet and describe it exactly. It is for this reason that we describe some of the twenty-five categories of ordinary expenses below.

### BUSINESS EXPENSES:

This does not include the work you do for your employer. It means a business that you have separate and apart from your everyday salaried employment. There are thousands of possible business ventures you may be engaged in. Whenever you have an expense where money of the trust is used to pay the expenses for the business or with respect to the business, call it a business expense. If you have more than one business, be sure that you write down the expense on your Trust Expenses Sheet which business it is against.

If bookkeeping does not scare you too much it would be a good idea for you to keep completely separate records of the income and expenses with respect to each business. It is not critical for you to be able to identify the different types of business expenses that are possible but be sure to describe the business expense as a business expense.

1. ADVANCE:

When the trustees use any of the money from the trust account or any other money of the trust for themselves personally, they must call such expenses an advance. Examples of this include money taken from the trust to buy food, personal entertainment, etc. Any other money paid for personal expenses falls into this category. The trustee must put this on his personal tax return.

2. AUTO EXPENSES:

Any vehicle owned or leased by the trust will have expenses. All expenses in running, repairing, and maintaining those vehicles are called auto expenses. Any expense whatsoever that has anything to do with the vehicles in the trust is called an auto expense.

3. BENEFICIARY DISTRIBUTION:

A beneficiary distribution is the distribution of money to a beneficiary. That is, when the trustees decide that, according to the terms of the trust indenture, it is wise to distribute money for the use of the beneficiaries. It only includes those amounts which are actually and formally approved as a distribution. If you feel it is necessary to make a beneficiary distribution, be sure you take the simple but formal steps necessary for the trustees to approve and record it in the trust minutes.

4. CONSULTING FEES:

Consulting fees are defined as money paid by the trustees to persons who act as consultants to the trust. The only time consulting fees are paid is when the trustees make a formal minute to that effect. That is consulting fees are earned as a matter of contractual relationship.

5. CHARITABLE CONTRIBUTIONS:

Any money or goods that you donate to charity constitutes a charitable contribution. This includes money paid to a

church, the Boy Scouts, United Way or any other recognized charitable organization. When you make a contribution to charity enter it in the bookkeeping category as, “contributions.”

6. CREDIT CARD PAYMENTS:

If your trust has a credit card you must be very careful to use it only for trust business. If your trust uses a credit card you must save your credit slips to indicate the nature of the purchase. To be extra safe, keep both the credit card slip and the monthly statement.

7. HOUSE EXPENSES:

The trust headquarters is the housing expense. That is, any mortgage payments to purchase the house or any rental payments made to rent a house constitutes housing expenses of the trust. House insurance will be included under the category of insurance.

8. INSTALLMENT PAYMENTS:

Installment payments are payments made for the purchase of an item which must be paid periodically over a long period of time. Do not include credit cards payments in this category.

9. INSURANCE:

This category is for all insurance, no matter what, except medical and dental. Remember to write down exactly what the expense is for. Certain types of insurance are fully deductible, such as insurance in connection with a trade or business. Some other types of insurance are auto, homeowners, and life (provided the trust is the beneficiary).

10. INTEREST PAID:

Any interest you pay to anyone for the use of their money or property as you are buying it, is deductible to a trade or business. Enter this carefully so your accountant can tell which are deductible and which are not.



11. MEDICAL AND DENTAL:

When trust money is paid out for a medical expense item, it is called a medical expense. But be very sure you document it exactly. Medical insurance is a medical expense.

12. PRIOR YEAR DISTRIBUTION:

This is a very complex category. We will not discuss it at this time. The best advice is for you to consult your accountant to determine how, when and in what amount to make distributions with respect to the prior year. Be sure to clearly mark any distribution made for the prior year.

13. REPAIR AND MAINTENANCE:

Any money paid for the repair or maintenance of the trust property comes under repair and maintenance. Any addition or improvements in the property of a permanent nature would come under capital expense. The word maintenance means, "to take care of." Therefore a maintenance expense is any expense necessary and proper for taking care of the trust property.

14. RENTAL EXPENSE:

Rental property is property the trust owns that is rented. Any reasonable or necessary expenses paid for that rental property is a rental expense. Just as we recommended, with respect to a business, we recommend you keep an entirely separate set of books for each rental property the trust owns. It is very important you specifically describe what the expense was for.

15. TAXES AND PROPERTY TAXES:

When you pay money to the federal, state or county governments for taxes, that is designated as taxes. When you write out the check to pay taxes, put down exactly what it was for. When you pay a tax you usually have some kind of a statement or bill from the government, that will tell you what kind of tax you are paying. If you are paying property taxes on property which is owned by the trust business, the tax

expense should be placed on the sheet pertaining to that business. Similarly, if you pay a tax on rental property that tax is an expense which should be placed on the tax expense sheet dealing with the rental property. If you don't know about the expense, just make sure that you describe the expense as clearly as possible on the trust expense sheet.

16. TELEPHONE AND UTILITIES:

All telephone and utility expenses for the trust property connected with trust business should be listed as utilities. If you can determine how much of the telephone bill is attributable to the business of the trust, be sure to designate that on the trust expense sheet. The utilities necessary for the administration and management of the trust are trust expense.

17. TRUST SUPPLIES:

The ordinary and necessary supplies purchased for the trust and the administration of the trust are a trust expense. Everything necessary for the caretakers or managers to carry out the functions to preserve, maintain and care for the trust, constitutes a trust expense. Food and any other expense for personal enjoyment or personal use by the trustees can never be an expense to the trust.

18. TRUST TRAVEL:

Travel expenses necessary to the trust are deductible items. If it is required for the trustees to go to a certain place, the travel expenses are deductible. It is very important that you carefully describe each travel expense and what it was for.

19. MISCELLANEOUS EXPENSES:

Any other expense that does not fall into one of the above categories is a miscellaneous expense. Again, be sure you describe exactly what it was so the bookkeeper can find a home for it.

**NOTE:** Sometimes you will be wrong in the decision you will make as to the bookkeeping category, and the accountant must have the description in order to correct that.

20. TRUST TAXATION:

A trust is treated as a separate entity for purposes of taxation, although it is really more of a contractual relationship between parties. In some ways it is treated as a corporation and a partnership. That is, the trustee function (the trust business) is taxed as a separate corporation, but distributions to beneficiaries pass through with the same type of tax consequences as in a partnership.

Since most of the more useful trusts are of the type called “complex”, it serves no use to tell how “simple trusts” are taxed. A complex trust is one where the trustee has discretion whether to distribute or accumulate the income or corpus of the trust.

Distribution to beneficiaries are deductible to the trust, and taxable as income to the beneficiaries. The distribution has the same character in the hands of the beneficiary as it does in the hands of the trust. So, if a capital gain is passed through, the beneficiary pays tax on the income realized by the sale of the capital asset, rather than ordinary income tax.

When the trustee holds back money from the beneficiaries (accumulates it), then distributes it later, the “throwback rules” will apply and the final tax result will be just as if the trustee had distributed the money to the beneficiaries when he first could have.

**NOTICE:**

Trusts cannot sell property used for depreciation purposes, essentially business property, within two (2) years of the time they receive it and get the favorable separate tax treatment they otherwise would get. This rule does not apply if the property was

sold or given to the trust for full fair market value. The rule taxes such a short term sale at the same rate it would have been taxed if the grantor held onto it. There are exceptions, and you should ask your trust technician about the use of Capital Gains Transactions.

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## **EIGHTH: DON'T OF THE BUSINESS TRUST**

If a grantor (creator or trustor) of a trust hangs on to too many powers over the trust when originally established, it will be treated as if there were no trust; that is, as if the property were still in their own hands. That would eliminate the income tax advantages of a trust, for all the income of the trust would then be taxed to the grantor. These dangerous powers are:

1. Property of the trust will revert to them within ten years.
2. Close relatives are the entire board of trustees.
3. The grantor reserves a power to determine distributions or benefits from the trust.
4. The benefits of the trust can flow to the grantor without the approval of an “adverse party.”
5. The income of the trust can be used to pay personal debts.

Such a trust is called a “GRANTOR TRUST” and all the income is taxed to the grantor or creator, not to the trust nor to the beneficiaries. Other dangerous powers include:

6. Power to revoke the trust.
7. Power for anyone to distribute the corpus or income to himself.
8. Power to use trust property to support someone the grantor is legally obligated to support.

Any of these dangerous powers can make the trust “GRANTOR TAXABLE.” Other dangerous powers include:

9. Power to deal with the trust for less than an adequate consideration.
10. Power for the grantor to borrow from the trust without adequate interest or adequate security.
11. Power for the grantor or non-adverse party to decide who gets how much of the property or income of the trust.

Some powers that are NOT DANGEROUS:

1. Power to distribute income or corpus to charity.
2. Power to distribute corpus limited by an ascertainable standard.
3. Power to accumulate income.

There are three devices that give more flexibility to trusts for tax purposes while appearing to restrict the grantor’s control over the trust:

1. The use of an INDEPENDENT TRUSTEE.
2. Providing that distributions must be made in accordance with a DEFINITE EXTERNAL STANDARD.
3. Providing that distributions must be approved by an ADVERSE PARTY.

When a person dies (e.g., the Grantor), none of the property of the trust is taxed in their estate. They do not own the property, the trust does. Consequently, the trust assets are not subject to either PROBATE or ESTATE TAXES. Giving the property to a trust in

the first place, however, can be taxed as a gift, unless the grantors hold all the unites of beneficial interest at first. Retaining “Strings of Control” by the grantor over the trust can cause the property to be taxed to their estate when they die as if they still owned the property.

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## **NINTH: BUSINESS TRUST MINUTES**

### MINUTES (SAMPLE):

The trust organization by the terms of its indenture is required to maintain minutes and records of its operation. This presents no great difficulty as minutes are simply the diary which relates to the decisions and acts of the trustees. The minutes should be kept in a book with letter size pages. A loose leaf binder is ideal, since it is important that, the minutes be preserved.

### **EVERY ACTION TAKEN BY THE BOARD OF TRUSTEES SHOULD BE RECORDED IN THE MINUTES.**

We highly suggest that you purchase "Trust Manager" Version 2.0.2 to aide you in keeping legal and legible minutes for your trust.

Trust Manager 2.0.2 can be purchased by calling toll free to 888-878-7860 or by lodging onto their web site at [www.trustsoftware.com](http://www.trustsoftware.com). You may also write to:

TRUST SOFTWARE & CONSULTING,  
5515 N. 7th Street, Ste 5-324  
Phoenix, AZ 85014

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**FIRST MEETING:**

This is your documentation that the meetings were in fact held, that the Board of Trustees met regularly, and that the trust was run in a business like fashion. Actually, having signed the Trust Indenture, the trustees and the grantor are having the first trustees meeting, to establish the trust. This meeting must be called by the grantor. The grantor will appoint someone to act as recorder. The first business at the meeting should be to establish the framework of the trust so it can conduct the affairs of itself. An example of a first meeting could be as follows:

May 24, 1989

At the first Trustees' Meeting, held at 7326 Willow Ave. City of Palo Alto, State of California, this meeting is called to order by the Grantor John Smith, and all that were invited are present and accounted for.

1. That upon the request of the Grantor, John Smith, on this date the following have been appointed Trustees in the J. R. & S. Holding Trust: Robert Adams a non-related trustee and Nancy Smith who is adverse. The above named persons, by their signing the trustee acceptance sheet of the trust indenture, show their acceptance of the duties, responsibility and assets of this trust.

2. That Nancy Smith shall occupy the position of Chairperson.

3. John Smith the Grantor now turns the Trust and all its assets over to the Board of Trustees.

4. The Board of Trustee~ now appoints Rose Smith who shall occupy the position of Secretary, Treasurer, and Recorder of the Trust Minutes.

5. That John Smith is hereby appointed to the position of General Manager, whose duties shall include, but not be limited to the buying and selling of property, investing of funds, borrowing and loaning of monies (except to himself), engagement of professional assistance and

the conduct of all the business of the Trust; subject to the approval of the Trustees. The General Manager shall engage competent accounting services and maintain or cause to be maintained adequate books and records of the operation of the Trust. A statement of the operations for each calendar year shall be presented to and be examined by the Board of Trustees at a meeting to be held not later than thirty (30) before or after the close of each calendar year. This statement of condition shall be incorporated into the minutes of such meeting, and then becomes the responsibility of the Trustees.

6. The Trustees may hold and conduct meetings at such times and places as best suit their convenience.

7. At such meetings where official business may be conducted, not less than two-thirds of the Trustees shall be present (in person or by telephonic conference) and participate in the meeting.

8. On this date the Trustees did receive from the Grantor certain real and personal properties as shown on schedules A and B, ("A" for real property and "B" for personal property), and attached to the trust indenture, and for this the Grantor received 100 Units of Beneficial Interest (UBI).

9. When a trustee objects to any of the minutes for any reason he or she must sign that minute and after his or her name write the word "dissenting" for future reference.

10. The Trustees are to execute the Bank Resolution Minutes and designate the Bank that is to be the depository for the trust funds (Use Bank Resolution Minutes sheet).

11. The Trustees shall immediately apply for the trust federal identification No. (use form SS-4), and Form 56 if the IRS requires it.

12. The next trustees meeting is to be held on December 3, 1990, at Stockton, California. All Trustees and officers are invited and expected to attend.



There being no further matters to bring before this board, it is motioned and second that the meeting be adjourned.

Time	Trustee	Date	Trustee	Date
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You will note that the first paragraph stated the date and location of the meeting and that all minutes are numbered. This numbering is for easy reference and to enable extract copy of minutes to be prepared so that you may give copy of minutes to outside third parties without having to reveal the entire business of the meeting. This is an example only and would vary according to the individual organization makeup.

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**SECOND MEETING MINUTES:**

At this, the second meeting of the Board of Trustees of the \_\_\_\_\_, trust held at \_\_\_\_\_  
City of \_\_\_\_\_, State of \_\_\_\_\_, all trustees being present, pursuant to minute 12 of the prior meeting the following decisions were reached:

13. The minutes of the first meeting were read and approved.
14. That pursuant to minute number 11, the SS-4 form was sent to the IRS and the trust federal identification number is \_\_\_\_\_. The IRS did not request form 56 so it was not sent.
15. The Trustees issued UBI's to John Smith 50 each and Rose Smith 50 each. They then asked the Board to reissue 10 UBI's from John Smith to his son Mark Smith, and 10 from Rose Smith to her daughter LeAnn Smith, which was completed on June 2, 1989.
16. That the Trustees shall see that adequate medical insurance be obtained for the UBI holders.

**NOTE:** Add other minutes as needed to carry on your duties as trustees to keep the trust running smoothly. All minutes must be numbered consecutively.

Next Number. The next trustees meeting is to be held on \_\_\_\_\_ 1991, at \_\_\_\_\_, or as the trustees shall direct.

There being no further matters to bring before this board, it is motioned and seconded that the meeting be adjourned.

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### **THIRD MEETING MINUTES:**

At this the third Trustee's meeting, held at \_\_\_\_\_ City of \_\_\_\_\_, State of \_\_\_\_\_ all trustees being present, the following decisions were reached:

Next number. Then go on with you minutes as they happen.

If you elect to purchase Trust Manager 2.0.2; you'll find the task of Minute Keeping a whole lot easier.

Trust Manager is a specialty administrative record keeping software program that helps you **record and keep track of minutes and documents for any type of trust**. In business since late 1995 with a proven support track history.

- Keep track of your **Minutes**. All meetings are automatically formatted for you.
- Comes with **private** trust minutes and documents which are extremely hard to come by.
- **Minute Library** with over **180 key sample minutes** already typed in and ready for use.
- Produce **documents** such as letters, contracts, and other trust agreements.
- **Document Library** with over **115 key sample documents** such as Lease Agreements, Contracts, Letters...etc. ready for use.

- Record **Inventory** with accumulated totals for each Trust and Category including a grand total for all trusts.
- A free add-on feature to Trust Manager called **Trust Manager Word Templates** has the capability of doing all your Documents directly in **Microsoft Word 95 or Microsoft Word 97** using either **Windows 95/98 or Windows NT**. It automatically ties into the Trust Screen using field and form with drop downs for easy use.
- **Track multiple Trusts**, Trustees, Successors, Beneficiaries, and Units of Beneficial Interest.
- **Search engine** that can find anything done to each individual minute.
- **Year 2000 compliant** - Trust Manager will handle year 2000 dates and always has.
- **Free support** for 90 days.

### **Subject Papers**

- **First Year Sample Minutes** - Key sample minutes for the first year for three different types of trusts
- **Why and how to do Minutes and Meetings**
- **Mission Statements** - Ideas on Mission Statements for all types of trusts with samples
- **Trust Installation Checklist** - to help you self install in trust
- Conveying Inventory - initial inventory taking
- **Security Issues** - hints on keeping information private
- Trust Manager Getting Results - for the novice to run Trust Manager
- Trust Manager Easy Steps - checklist for using each screen in Trust Manager
- Platform and Software Suggestions - Standard Software and Platform Suggestions

## **TENTH: BUSINESS TRUST TERMS**

"Acceptance of the Trust" is an agreement, either expressly or by contract, where a person acts on behalf of another. All parties become legally bound to the Trust/Contract by their acceptance. By accepting the trust, the trustee consents to occupy that position and carry out the duties set forth within the trust instrument, subject to the laws of fiduciary responsibility.

"Acknowledgment" means the admission, concession, confession, or avowal of existence of the trust of anything. In law, an official certification in legal form, admission of a debt or other liability.

"Adverse" [party] is defined as any person (1) who has a beneficial interest in the trust; (2) whose beneficial interest is "substantial"; and (3) whose interest would be adversely affected by the exercise or non-exercise of the power or interest held by the Independent Trustee or other person in question.

"Advisor" includes any advisory Trustee, agent, investment advisor, or legal adviser employed pursuant to the terms of this deed.

"Affirm" is to declare to be true, say firmly, assert, aver, maintain, or avouch.

"Agreement" is a valid contract in which a complete understanding is reached by two or more persons, groups of persons, etc.; often called a "meeting of the minds."

"Assistant Manager" is a person, natural or juristic, chosen to run a business or a portion of a business.

"Beneficiary" of a trust is the person(s), natural or juristic, for whose benefit the property is held in trust.

"Beneficial Interest, Units (UBIs)" are merely the rights to enjoy the monetary profits, or other physical benefits, resulting from a trust,

contract, estate, or property rather than the legal ownership of these things; thus providing a more flexible way for the identification of the beneficiaries. Units of beneficial interest are transferable with some very important restrictions and exceptions; therefore, the "beneficial interest" of the trust can be easily shifted from one person to another without complexity. Initial UBI holders, with their number of units, are recorded within the trust in the Registry. Beneficiaries may then transfer all, or some, of their Units simply by filling out the reverse side of their "evidencing certificate" and surrendering the Certificates to the Trustee for re-issue. More precise procedures are outlined within this Agreement.

"Common Law, Federal" is Judge-made law as defined by the courts, which consists of those principles, usages and rules of action applicable to government and security of persons and property which do not rest for their authority upon any express and positive declaration of the will of the legislature-made law (*Bishop v. D.C. Tex.*, 334, F. Supp. 415, 418). As mandated by the U.S. Supreme Court in United States v. Marchant, 25 U.S. 480, 12 Wheat. 480, 6 L. Ed. 700., "The courts of the United States are bound to recognize and enforce the common law."

"Company" means any corporate body or partnership, of whatsoever kind, incorporated or otherwise brought into existence anywhere in the world for the purpose of doing business.

"Consideration" is something given or done as a return for something given or done by another, without which no contract is binding. It is the main reason or cause for a person to make a contract.

"Constitution, United States" was the second Law of the People, being ratified on September 17, 1787 by We the People, not we the government, nor we the congress, or we the judges. It is the basic law of America, on which most other laws are based, and to which all other laws must yield.

"Contract" is an agreement that affects or creates legal relationship(s) between two or more persons. To be a *contract*, an agreement must involve: at least one promise, consideration (something of value promised or given), persons legally capable of making binding agreements, and a reasonable certainty about the meaning of the terms.

"Contract Clause" is the provision in Article I of the United States Constitution that no state may pass a law abolishing contracts or denying them legal effect.

"Conveyance" is a transfer of ownership, the document showing such a transfer, or a deed, from an individual to the Trust.

"Corpus" of the trust is one of the essential requirements for the establishment of the trust. No trust can exist without property (corpus). The property can be real or personal property of any type.

"Creator" is an individual or juristic person who initiates the formal process of creating the Trust and directs or carries on the technical process by which it is achieved.

"Declaration of Independence, The" was written to declare the authority of the citizens of the colonies in 1776, being later totally adopted as the standard by which to protect the Laws of Equality/Common Law and the Inalienable Rights of We the People. With this document, the United States Federal Common Law, the Law of Equality, became, in fact, the first statement of Common Law ever written for a nation, thence the world's first written Common Law.

"Declaration of Trust" is a written statement formality by a person owning property that is held for another person. It makes clear the fact that a trust is created and not some other kind of organization or transaction.

"Domicile" is the legal residence of the Trust or any individual or juristic person which determines the laws which apply to matters affecting the Trust, individual or person.

"Emergency Trustee" means the person named or any such other person as may be appointed or become the Emergency Trustee in accordance with this Agreement.

"Equity" is justice administered by the courts according to fairness when existing laws do not cover some situation of person's rights being violated as contrasted with the strictly formulated rules of common-law.

"Excluded Persons" means all and any of the persons specified herein or otherwise becoming an Excluded Persons under the provisions of this Agreement.

"Form" is the legal or technical manner or order to be observed in legal instruments or juridical proceedings, containing the proper technical terms or phrases and in proper and methodical order.

"Indenture" is the most important guide you will ever have in running and operating the trust. The trust indenture determines who can do what, how, where, why, and when. The indenture can also state restrictions or forbidden acts. The indenture may also state acts or actions that must be done with no deviations from the indenture's instructions.

"Independent Trustee" is a trustee who has an opposing interest from that of the grantor/creator and could therefore, be expected to oppose any special or self-serving interest being given to the grantor/creator as opposed to the beneficiaries at large; e.g., any person not related by blood, marriage, or employment to the grantor/creator.

"Infant" means any individual who has not attained the age of twenty-one years, notwithstanding that such individual may in accordance with the law of his or her domicile be of full age.

"Insolvent" denoted inability to pay one's debts, bankrupt, having liabilities far greater than one's assets.

"Juristic Person" is a legal entity created by law rather than by nature but still having many of the same rights, privileges, freedoms, obligations, and responsibilities of a natural person. A corporation is a juristic person.

"Limited Partnership" is a special form of unincorporated business organization ownership, available under most state laws, that allows the business to be run (managed) by general partners and financed (investors) partly or fully by limited partners, who may take no part what-so-ever in the partnership management and therefore have no liability for business losses, lawsuits, etc., beyond the amount of money they invested, or promised to invest, in the partnership.

"Manager" is a person, natural or juristic, chosen to run a business or a portion of a business.

"Minutes" are written notes which record the events of Trustee meetings. No special format is required, however, the more detailed the minutes, the better is the piece of documentary evidence will exist.

"Non-adverse" [party] is defined as any person who is not an adverse party to the trust.

"Person, Natural" means any individual or any body of persons corporate or unincorporated.

"Protector, The" shall mean the person, persons, or corporation, for the time being, holding the office of Protector in accordance with Schedule "I" to act as a Protector, or such other individual or company which may be appointed, or become the Protector, in accordance with this Agreement.

"Quorum" is the number of members of any assembly required that must be present in order for business to be legal or binding.

"Related" or subordinate [party] is defined as any person who is also a member to the grantor's/creator's family or related to the



grantor/creator through certain types of business contracts; e.g., being related by blood, marriage, or employment to the grantor/creator.

"Substance" is that which is essential, ensures the "*form*" is accountable, and meets all requirements.

"State Laws" determine how a trust is created, administered, and how people are to act with respect to the trust. These laws are based upon the Common Law of England, being very similar throughout the United States. Although Federal law determines the test for taxing trusts, state law determines what the property rights or interests are in order to apply those taxation tests.

"Statutory Law" consists of Federal, State and Local Statutory and Regulatory authority created by U.S. or State Constitutional Mandate, or the Charter of a municipality to regulate the government and to create the guide lines for the governments limitations with regard to the protected civil rights of private citizens. Statutory entities (i.e., corporations, associations, partnerships, statutory trusts, sole proprietors, etc.) are creatures of the state and owe their existence and charter power to the State. They are presumed to have been created for the benefits of the public and therefore do not have rights such as the individual.

"Trust" is a contract between two or more parties, natural or juristic.

"Trustees, Board of" means the official body appointed and organized by the Creator/Grantor consisting of the Original Trustees or other trustee or trustees including Emergency Trustees as are appointed or become trustees in accordance with this Agreement. The Board of Trustees is only answerable to the beneficiaries through the proper court, the beneficiaries having no power over the trustees.

"Trust Fund" means:

- (a) The property specified in the Schedule "A" and "B" hereto;
- and

- (b) All money investments or other property hereafter paid, transferred, or delivered to or otherwise placed under the control of and (in any such case) accepted by the Trustees as additions to the Trust Fund; and
- (c) All assets, accumulations of income, capital accretions or otherwise derived from the property specified under Sub-clauses (a) and (b) of this definition.

Any references to the income of the Trust Fund shall (without an allocation or apportionment in favor of the Settlor) extend to any income now accrued or accruing but not yet actually payable in respect of the Trust Fund.

"Trust Period" means the period commencing with the date of this Agreement and ending on the first to occur of the following dates, namely:

- (a) The date of the one hundredth anniversary of the date of this Agreement;
- (b) The period commencing on the execution hereof and continuing until such day as the Trustees with the consent of the Protector may by deed or written declaration at any time and at their discretion declare to be the date of the expiration of the Trust Period. Notwithstanding the foregoing, the Trustees shall have no authority to shorten the duration of the Trust Period if such act is the result of any compulsion or Event of Duress.

"Voluntary Compliance" is not created directly by a license, but by the appearance of license based on the attempt of a citizen to comply with statutes and regulations that may not require the citizen's compliance. The Courts have ruled that "A citizen is under no obligation to do any particular thing. A citizen's failure to act creates no liability, but if a citizen voluntarily attempts to act and do the particular thing the citizen comes under implied obligation in respect to the manner in which the citizen does it." Waivers of Constitutionally protected rights not only must be voluntary, but must be knowingly intelligent acts done with sufficient awareness of relevant circumstances and consequences.

## APPENDIX “A”

### SETTING UP THE TRUST BOOKKEEPING

It is important that the Trust bookkeeping is set up and done properly in order to preserve the Trust and its assets. This booklet has been written to make your job easier, both now, and should the need arise, to act as proof of the operations of the Trust. Paperwork is IMPORTANT!! It is your audit defense. the Trust is a separate Entity, like a corporation. You cannot use the bank account as your personal checkbook. All funds must be accounted for to your employer, the Trust and to it's Trustees. The Trust must be on a calendar year with tax returns filed on that basis. New state ID numbers must be obtained for payroll and sales tax needs. Personal property tax statements will now list a lease from the Trust that holds the equipment for the business at the new value and you will need to se~up a lease,, payment schedule. You are a new business and will need a new business license with the city or county.

The investment you have in the trust is important and must be protected. It is your responsibility to do the job and do it correctly, so that the trust can continue under the terms of the trust documents.

#### INITIAL ASSETS:

##### 1. How to value initial assets.

A) Real Estate: If the property was recently purchased, then the cost of the property is the most likely amount to use. Structures must be separated from land as land is not depreciated. Use the property tax statement to break down the land and structures. If you have held the property for a period of time, get a real estate appraiser or real estate agent that can give you comparable sales and a good estimate of the value of the property.

B) Equipment: If equipment has been purchased recently, cost can be used. If the equipment is readily in demand, then a fairly high value can be placed upon, the equipment. You can check with used equipment dealers as to what they would sell the equipment for. A quick rule of thumb may be a value of fifty percent of what you originally paid for it, subject to the above considerations. You would not be able to take Section 179 (fast write-off of equipment up to

## APPENDIX “A”

\$10,000 in the year of purchase) since you would possibly be considered' the same user.

C) Autos: High blue book or recent purchase price.

D) Goodwill: Your business may have a value that can be placed upon it, if you were to sell it. There are people that can give you an estimate of the selling price. Though this item can not currently be depreciated, it can increase the basis of the business should you plan to sell in the future and thereby decrease the taxable gains of the sale.

E) Supplies: Most businesses have a small amount of office or shop supplies on hand at the beginning of the Trust. You can estimate what you paid for these items so that they can be written of f in the Trust.

F) Inventory: If you are in the type of business that has a substantial amount of inventory, you should have a'n inventory service come in and do an inventory for the start of the Trust. If you can price items from cost, then you can do your own inventory.

G) Other Intangible Assets: Covenant Not To Compete (if carried to the Trust), Copyrights, patents, etc. Transfer at cost or book value. Start up expenses were for the previous business only and would not be included here.

H) Investments: Common Stocks, Bonds and Mutual Funds can be set up with the current market price. Call your broker and look in the daily paper.

I) Partnerships and Small Corporation Stock: For a partnership, you will need to get the current listing of assets and liabilities and using the above suggestions, arrive at a current worth of the partnership and multiply that by your percentage of ownership. The same would be true for the Corporation and your share would be based upon the number of shares of stock you hold verses the number of shares issued by the Corporation.

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J) Liabilities: Loans transferred to the Trust would be picked up at their remaining balance.

### TYPE OF BUSINESS:

#### SERVICE BUSINESS:

A Service Business is normally run on a cash basis; that is, when money is received, it is reported as income and when bills are paid, it is an expense. This does give you some room for tax planning by delaying receipt of income and prepaying expenses in order to reduce taxable income, or vice versa. Your income can be reported in several different accounts for your planning purposes. You normally would not have cost of goods sold accounts. You would have normal asset and liability accounts as needed. The capital account would be in the Trust name. There would be no draw accounts, only distribution accounts. Reserve accounts would be set up as needed. A typical chart of accounts would be as follows:

#### Assets:

- 102 Petty Cash
- 103 Cash in Bank
- 104 Cash in Second Bank (as needed)
- 149 Accounts Receivable Employees
- 165 Prepaid (Rent, Insurance, etc.)
- 185 Operating Capital Reserve

#### Liabilities:

- 302 Loan
- 335 Employee Federal Income Tax Withheld
- 337 Employee State Income Tax Withheld
- 341 Employee FICA Tax Withheld
- 343 Employee SDI Withheld

#### Equity:

- 431 Distribution to Beneficiary (Name)
- 433 Trust Capital

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490 Trust Retained Capital

### Income:

501 Service Income

517 Returns Allowance

525 Interest Income

### Operating Expenses:

801 Advertising

802 Accounting

807 Auto

811 Bank Service Charges

813 Cash Short & Over

815 Commissions

817 Contributions

821 Delivery

825 Dues & Subscriptions

827 Entertainment

829 Equipment Rental

831 Interest

833 Insurance

835 Janitor

837 Laundry & Cleaning

839 Legal

841 Licenses

843 Maintenance & Repairs

844 Medical

845 Miscellaneous

847 Office Supplies

853 Postage

855 Professional Fees

857 Promotional

858 Rent

863 Payroll

864 Shop Supplies

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- 867 Sales Tax
- 868 Services
- 869 Payroll Taxes
- 871 Other Taxes
- 875 Telephone
- 876 Meals
- 877 Travel (Commercial Travel and Lodging)
- 879 Utilities
- 890 Trustee Expenses
- 905 Non Deductible Expenses (penalties & fines) and other accounts as needed.

### SALES/STORE/MANUFACTURING:

These additional accounts would be needed.

#### Assets:

- 153 Inventory

#### Income:

- 510 Sales Tax Received

#### Cost of Goods Sold

- 653 Purchases

### EQUIPMENT MANAGEMENT BUSINESS:

This Trust holds the equipment. for the Business Trust. This Trust would operate on a cash basis. This is where you would want to set up a reserve for purchasing new equipment or for buying our business building. The accounts you may need are as follows:

#### Assets:

- 103 Cash in Bank
- 185 Operating Reserve (Equipment)
- 209 Furniture & Fixtures
- 210 Equipment
- 211 Automobiles

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- 219 Accumulated Depreciation Allowance - Furniture & Fixtures
- 220 Accumulated Depreciation Allowance - Equipment
- 221 Accumulated Depreciation Allowance - Autos
- 271 Leasehold Improvements.
- 272 Amortization Allowance - Leasehold Improvements
- 275 Buildings
- 276 Accumulated Depreciation Allowance - Buildings
- 279 Land

### Liabilities:

- 302 Loan
- 303 Loan
- 304 Loan
- 305 Loan

### Equity:

- 431 Distribution to Beneficiary (Name)
- 433 Trust Capital
- 490 Trust Retained Capital

### Income:

- 501 Lease Income
- 509 Distribution From Trust
- 525 Interest Income

### Expenses:

- 823 Depreciation
- 831 Interest
- 890 Trustee Expenses

### REAL ESTATE RENTAL BUSINESS:

This trust holds real estate rental property; preferably only one property per trust. The trust operates on a cash basis. You should not use a reserve account in this trust to purchase other real estate. You may wish to maintain a small reserve to handle repairs, maintenance and operating expenses. You could make this equal to the depreciation deduction or a portion of it. The idea is to limit the exposure



## APPENDIX “A”

to someone suing the trust for its assets. The accounts you may need are as follows:

### Assets:

- 103 Cash in Bank
- 185 Operating Reserve
- 209 Furniture & Fixtures
- 219 Accumulated Depreciation Allowance - Furniture & Fixtures
- 271 Leasehold Improvement~
- 272 Amortization Allowance - Leasehold Improvements
- 275 Buildings
- 276 Accumulated Depreciation Allowances - Buildings
- 279 Land

### Liabilities:

- 302 Loan

### Equity:

- 431 Distribution - Beneficiary
- 433 Trust Capital
- 490 Trust Retained Capital

### Income:

- 501 Rental Income
- 502 Miscellaneous Income
- 509 Distributions From Trust

### Expenses:

- 801 Advertising
- 802 Accounting
- 807 Auto
- 811 Bank Service Charge
- 815 Commissions
- 823 Depreciation
- 825 Dues & Subscriptions

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- 829 Equipment Rental
- 831 Interest
- 833 Insurance
- 837 Laundry & Cleaning
- 839 Legal
- 841 Licenses
- 843 Maintenance & Repairs
- 845 Miscellaneous
- 864 Supplies
- 868 Services
- 871 Property Taxes
- 875 Telephone
- 877 Travel
- 879 Utilities
- 890 Trustee Expenses

### **NOTE:** [Sale of Primary Residence:](#)

Tax rules generally permit a \$500,000 (married filing jointly) or \$250,000 (single or married filing separately) exclusion on the gain from the sale of a primary residence. If part of the home is used for business purposes, the gain is divided into two parts -- the personal-use portion (the exclusion applies) and the business-use portion (exclusion does not apply). For example, a taxpayer who qualifies for the exclusion, but has used 25 percent of the home for business purposes during the during past five years, will only be able to apply the exclusion against 75 percent of any gain recognized on the sale of the home.

### ASSET MANAGEMENT BUSINESS:

This is the Trust that would hold your residence and/or furniture. It could hold your business assets if you ‘do not have an Equipment Trust. This Trust would pay your medical expenses (insurance and possibly a medical reimbursement plan), life insurance, auto expenses and home expenses. This is a Trust that would hold your investments and reserves for various needs such as a Scholarship Fund. Also, this is the Trust that gives you your distribution (taxable & non-taxable). The accounts you could use are as follows:

Assets:

- 102 Petty Cash

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103 Cash in Bank  
185 Operating Reserve  
186 Investment Reserve  
209 Furniture & Fixtures  
211 Automobiles  
219 Accumulated Depreciation Allowance - Furniture & Fixtures  
221 Accumulated Depreciation Allowance - Autos  
271 Leasehold Improvements  
272 Amortization Allowance - Leasehold Improvements  
275 Buildings  
276 Accumulated Depreciation Allowance - Buildings  
279 Land

### Liabilities:

302 Loan

### Equity:

431 Distribution to Beneficiary (Name)  
432 Distribution to Beneficiary (Name)  
433 Trust Capital  
490 Trust Retained Capital

### Income:

509 Distribution from Trust  
525 Interest Income  
526 Dividend Income  
527 Partnership Income

### Expenses:

807 Auto (Gas)  
811 Bank Service Charge  
817 Contributions  
831 Interest  
833 Insurance  
837 Laundry & Cleaning

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- 843 Maintenance & Repairs
- 844 Medical
- 845 Miscellaneous
- 858 Rent
- 864 Supplies
- 868 Services
- 871 Property Taxes
- 875 Telephone
- 876 Meals - Travel
- 877 Travel (Commercial Travel and Lodging)
- 879 Utilities
- 890 Trustee Expenses

### ESTABLISHING RESERVES:

A reserve fund can be set up for most any reason per the minutes of the Trust. Some of these Reserves could be taxable to the trust while some are tax deductions. Some of the different types of reserve funds are as follows:

An Operating Reserve to pay trust expenses helps to keep sufficient cash on hand to pay the bills and obligations as you grow.

An Equipment Reserve could be established to purchase new equipment or to replace old equipment.

A Depreciation Reserve to allow for the depreciation (all or part) to stay in the trust to cover unforeseen needs.

A Building Reserve to pay for a building for the business.

An Investment Reserve which adds to the corpus and can be invested for the future. This can be stocks, bonds, mutual coins, rare coins and other collectibles and investments.

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A Reserve for a Scholarship can be set up in advance to help cover education expenses for the recipient of the scholarship or you can fund it as you go along.

A Reserve for Gifts to be made at some future date. Clearly document in the trust minutes what is to be done and then carry it but in the accounts of the trust.

### LOANS:

Any loans to anyone needs to be documented in the minutes and **set up** on the books. A reasonable interest rate and period of time for payment and payment amount needs to be determined.

### DISTRIBUTIONS:

These can be any time funds are distributed. They can be non-cash distributions. The minutes should document any unusual distributions.

## **MONTHLY TRANSACTIONS AND REPORTS**

The bookkeeping needs to be done on a regular monthly basis in order to be able to properly run the Trust. You need to make monthly and year-to-date profit and loss statements and a balance sheet of the assets, liabilities and equity of the Trust. A manual bookkeeping system can be kept; however, it is much easier to keep the books on a computerized system. It also helps in providing the financial statements for the bank or others as needed.

## **YEAR END REPORTING AND CONSIDERATIONS**

You need to complete your bookkeeping as soon as possible after the end of the Calendar year (Trusts must report on a Calendar year end basis). You have 65 days after the end of the year to distribute any remaining funds from the Trust in order for the Trust to avoid paying any taxes. This may be the time to set up reserve accounts in your planning.

## APPENDIX “A”

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## **APPENDIX “B”**

This document may not cover all possible activity that you could have in your Trusts; however, it should be a guide of what to do for the normal activity you may encounter. It is hoped that it will give you a good starting point in accounting for your Trust.

### **TERMINATING THE OLD BUSINESS**

The old business still has some' obligations to complete before it is done with. You may have payroll taxes and reports and sales tax and reports to file. The W-2's and year end tax reports also need to be reported.

Depreciation can be used through the last month in the old business and since the assets were not sold, there would be no recapture of Section 179 (up to \$10,000 fast write-off of equipment).

If the Trust did not assume the old liabilities and receivables, you would have that to continue with there as well.

Income tax returns also need to be filed for the old business. A sole proprietor reporting on Schedule C on their tax return. A partnership would report a final return on form 1065. A corporation would be liquidated and any income taxed to the stockholders.

### **TRANSFERRING TRUST ASSETS**

There will be certain actions that will need to take place for those assets being conveyed to the Trust. These actions will convey title or ownership to the Trust entity from you personally. This is an important step in ensuring that the substance and accountability of the entity is correct and intact.

#### **REAL PROPERTY**

Reconveying or recording of property (residences, rentals, unimproved land, etc.) will be completed by submitting deeds (grant, warranty, etc.) and other county or state required documents to your county recorders office and paying appropriate fees. It is important to remember that each county in each state can be somewhat different.

## **APPENDIX “B”**

For instance, in California, there is a requirement that a "Preliminary Change of Ownership Report" be attached to every submitted Grant Deed, Correctory Deed, etc. Even though there is an approved State form covering all 58 Counties, some Counties are putting the form on different colored paper, changing the type face, and requiring use of their form instead of the state approved form.

Property taxes are a major source of revenue in all states. It is not uncommon to find a government agency attempting to collect taxes by a reassessment when any type of transfer takes place. Requirements for recording properties in some counties are changing almost monthly. Be aware that you may get something back from the County Records Office requesting additional information, or completion of another form. Should you get something like this, mail or fax the form along with a copy of the appropriate deed to Baldwin Trust Group. We will make every effort to walk you through the process.

In California, Baldwin Trust Group fought long and hard to get subparagraph “d” added to Section 11925 of the State’s Revenue and Taxation Code. If this transfer is ONLY a change in the way of holding ownership and the percentages of ownership (or benefit) did not change before or after the transaction; Section 11925(d) exempts the transfer/exchange from “Documentary Transfer Tax.”

## **PERSONAL PROPERTY**

Personal property is reconveyed to the Trust through an inventory list, and by making use of the "Schedule B" form that has been made available to you. In addition to listing this property, we recommend to include things such as photos, video recordings, and or any ID. numbers/serial numbers. Remember, any items placed in trust are now Trust Property, and therefore accountable to the Trust through the Trustees of the Trust Entity. For instance, if you convey an antique cabinet to the Trust, and it will be sold; the Trustee(s) must approve the sale by constructing a Minute and authorizing the sale of that item. Accountability, or substance of a Trust, is imperative should there ever be any question of the Trust. All monies from the sale of trust property must be returned to Trust (a check made out to the Trust) and deposited in the Trust account.



## **APPENDIX “B”**

When conveying personal property to the Trust make sure of the following:

The inventory list is complete (Schedule "B").

It is dated.

The Trustee(s) accept the inventory list (Schedule "B") into the corpus of the Trust .

This means a meeting must be held and a Minute written accepting the inventory list (Schedule "B").

Example...

*Meeting #3- Use a start of meeting form and complete all information required*

*Minute #27-(Remember Minutes are chronological)*

*The Board of Trustees of XYZ LTD, hereby accept the inventory list (Schedule "B") dated \_\_\_\_\_, into the corpus of the Trust in accordance with Article \_\_\_ and \_\_\_ of the Trust Indentures.*

## **EQUIPMENT**

Equipment is also conveyed to the Trust through an inventory list (Schedule "B"). This list needs to be handwritten and each item described specifically.

For instance:

The Manufacturer

The Model

The ID number

Inventory lists (Schedule "B") are also helpful for insurance purposes.

## **APPENDIX “B”**

This list also needs to be accepted by the Trustee(s) into the Corpus of the Trust. A Minute must be prepared and can be similar to the example given under personal property.

### **NOTES/DEEDS OF TRUST/LIMITED PARTNERSHIPS**

Concerning notes and deeds of trust; you have the option to make the trust the beneficiary of any notes and/or deeds of trust and/or to change the owner of the notes and deeds of trust. The recommended owner being the Trust; making the trust the owner and/or the beneficiary.

The request for either change must be a formal written request. A copy of the request along with the formal response indicating that the change has been made must be accepted into the Trust by the Board of Trustees through a Minute.

If the change is made to any notes and/or deeds of trust so that the Trust is the owner and the beneficiary; all future checks need to be made payable to the Trust and in the name of the Trust, and deposited into the Trust account only.

If the Trust is only being named as beneficiary of the notes and/or deeds of trust; then changing the owner of the notes and/or deeds of trust will not be necessary.

Example...

*This is a formal request that notes currently held in the name of Jane A. Doe be changed to XYZ Limited, Identification Number 97-9949494, Paula A. Smith, Trustee.*

*In addition, please change the beneficiary on all notes from Jane A. Doe to XYZ Limited, 222 Main St., Sunnyvale, Texas, 22222.*

*Thank you for your kind attention in this matter. Should you have any questions, contact me at (222) 232-5555*

*Sincerely,*

## **APPENDIX “B”**

*Jane A. Doe*

*Identification Number: 544-22-2323*

### **STOCK AND BONDS**

Stocks and bonds also have the same options as Notes/Deeds of Trust/Limited Partnerships. This means you can:

Make the Trust the owner and the beneficiary; or

Make the Trust only the beneficiary.

Either type of request must be formal and in writing. Copies of the request and response must again be accepted into the Trust through the Minutes and copies of each attached as “exhibits”.

You should also make a formal request in writing to the Broker that the stock value will be analyzed on the day of your request to establish a benchmark value of the particular stock. This benchmark is important for later sale of the stock or purchase of new stock.

This analysis by the broker must also be in writing and accepted into the Trust by Minutes signed by the trustees.

Example...

To: Pacific Gas and Electric

*To whom this may concern;*

*Please find enclosed a Stock Certificate and Irrevocable Stock or Bond Power. Please transfer ownership as shown on the stock power, and send the certificate to the trustees at the following address;*

## APPENDIX "B"

*Mr. and Mrs. John G. Smith, Trustees  
2345 North Meadow Lane  
Palm Springs, Ca. 95033*

*Sincerely,*

*John G. Smith Mary A. Smith*

*The Irrevocable Stock or Bond Power shows that the current person listed on the stock does hereby sell, assign, and transfer to the XYZ Limited Trust dated \_\_\_\_\_ day of 20\_\_\_\_, the number of shares of Stock, the certificate numbers of stock, and that is Pacific Gas and Electric stock, It is signed by the person executing this power.*

You should request the appropriate paperwork from the Broker. This may be different from one Brokerage house to another. Make sure you complete all the required paperwork along with a formal letter requesting the changes you wish to make.

### MUTUAL FUND HOLDINGS

The Trust can also be named as beneficiary, or owner and beneficiary, of any mutual funds you currently hold. Again, these request must be formal and be in writing. The request and response must be accepted into the Trust though Minutes signed by the Board of Trustees.

Example...

*This is a formal request that funds held in account number \_\_\_\_\_, currently held in the name of John Doe, be changed to \_\_\_\_\_, Trustee for \_\_\_\_\_ (Trust ID)\_\_\_\_\_.*

*In addition, please change the beneficiary on the account to \_\_\_\_\_ Trust, 2222 Jones Lake Rd, Little Rock, Arkansas, 30333*

## **APPENDIX “B”**

*Thank you for your kind attention to this matter. Should you have any questions, call me at \_\_\_\_\_.*

*Sincerely,*

*John Doe*

*Identification Number 333-33-3333*

### **INSURANCE**

In an active trust (general contract trust); the Trust can be named the beneficiary of the Insurance policy. Again, this should be a written, formal request changing the beneficiary from the current person listed to the name of the Trust entity.

In a business trust entity; the insurance policy should be changed from its current status making the Trust the owner and beneficiary of the policy. A letter as has been shown above can be written. Once this change is made in the business entity, insurance premiums can be paid out of the Business Trust Account.

The request letter and response letter must be accepted into the Trust by Minutes signed by the Board of Trustees.

### **AUTOS/RECREATIONAL VEHICLES/MOTORCYCLES**

Changing ownership of this type of property differs greatly from state to state. Most transfers are simple while in California the procedure has become awkward at best. Since the states tend to revise requirements without warning; it is always best to check beforehand with your State's Department of Motor Vehicles regulations before proceeding with any change of ownership.

*NOTE: Be sure you are familiar with the reasons for transferring such properties to Trust. "Rolling" property tends to run over and into people who like to sue. These kinds of property add in liability trails and could lead to disastrous financial results if there are valuable assets sharing the same Trust corpus.*

## **APPENDIX “B”**

**(California)** The California Department of Motor Vehicles does not require a vehicle to be owned outright before it can be transferred into Trust but if any encumbrances are owed against it; the DMV will make you go through the State’s Board of Equalization for their approval of the transfer. The Board of Equalization functions as clearing point on behalf of the DMV to ensure "no sale" has taken place (which means a sales tax would be imposed), and completes documentation for DMV processing. DMV removes title and transfer fees from you and issues new paperwork to the Trust.

**(Other States)** Most other states will transfer title whether the vehicle is paid for or not. Be sure to check with your local DMV before proceeding.

Once you understand the procedures of transfer, it is a relatively easy process.

## APPENDIX “C”

# TRUSTEE LIABILITY PROTECTION PROVISIONS

The following is a brief outline of the extent of the liability, or lack thereof, for trustees in the event a Common-law Contract Trust is sued by a would-be judgment creditor.

The first source of law to review in regard to the liability of trustees is the California Probate Code. Let’s therefore consider Probate Code Sections 15001 and 15002, which state:

15001. Except as otherwise provided by statute:

(a) This division applies to all trusts regardless of whether they were created before, on, or after July 1, 1987.

15002. Except to the extent that the common-law rules governing trusts are modified by statute, the common-law as to trusts is the law of this State.

The common-law is the case law of a State as opposed to its statutory law counterpart. As is evident from Section 15002; case law will apply except to the extent it has been modified in any way by a statute. There are a few other statutes which have modified case law, or which will be applicable in all circumstances; the first of which is Probate Code section 16011 which basically says that the trustees have a duty to take reasonable steps to defend actions that may result in a loss to the trust. This is fairly self explanatory, and doesn't really connect to trustee liability, but it does specify that the trustees have a duty to defend any such actions that may result in a loss to the trust.

There are other specific code sections which do touch on the liability of trustees to third persons. The first is Section 18000 of the Probate Code:

18000. Personal liability of trustee to third persons on contracts.

(a) Unless otherwise provided in the contract or in this chapter, a trustee is not personally liable on a contract property entered into in a trustee's fiduciary

## APPENDIX “C”

capacity in the course of administration of the trust unless the trustee fails to reveal the trustee's representative capacity or identify the trust in the contract.

The trustees avoid any possibility of liability by making sure that when in enters into any contract, actual or implied, it, the trust, specifies that the trust is a party to the contract and the trustees are acting in their fiduciary capacity as trustees on behalf of the trust. For background information, this changes the prior case law in California, which stated a trustee was personally liable on a contract unless the contract stipulated that the trustee was not liable. The cases in California setting forth this prior law are Hall v Jameson, 151 Cal. 606, 611-612 (1907), Duncan v Dormer, 94 Cal. App. 218, 221, (1928), cf. Purdy v Bank of America, 2 Cal. 2d 298, 301-302, (1935) [*trust estate also liable when properly bound by acts of trustees*].

With all of the foregoing in mind, it is important to also be aware of sub-paragraph (b) of Section 18000 of Probate Code which states:

(b) The personal liability of a trustee on a contract entered into before July 1, 1987, is governed by prior law and not by this section.

Thus, the case-law rule governing a trustee's personal liability for pre-operative date contracts has been preserved by Probate Code Section 18000(b); so for any contract entered into by a trust before July 1, 1987, the case law is applicable, and the trustees will be personally liable on a contract unless the contract stipulates that the trustees were not liable.

To reinforce the foregoing is a quote from Section 25.01 of Trust Administration & Taxation, Nossarnan & Wyatt:

25.01 As a general rule under the common law of trusts, the trustee is personally liable on contracts made on behalf of the trust. This rule has been revised in California by its Trust Law (effective July 1, 1987), providing now that a trustee is not personally liable under a contract properly entered into in the fiduciary capacity of trustee in the course of administering the trust unless the trustee fails to either reveal representative capacity or identify the trust in the contract.



## APPENDIX “C”

The next code section we want to consider is California Probate Code Section 18001, which states:

18001 Personal liability of trustee arising from ownership or control of trust estate. A trustee is personally liable for obligations arising from ownership or control of trust property only if the trustee is personally at fault.

A trustee is "personally at fault" when the trustee, either intentionally or negligently, acts or fails to act.

Let's briefly look at California Probate Code Section 18002:

18002: Personal liability of trustee for torts. A trustee is personally liable for torts committed in the course of administration of the estate only if the trustee is personally at fault.

In this particular area of the law, a trustee is "personally at fault" when the trustee commits a tort either intentionally or negligently. Cf. Johnston v Long, 30 Cal. 2d 54, 62-63, (1947):

Section 18004 of the California Probate Code indicates that any kind of an action against the trust has to be brought against the trustee in the trustee's capacity as trustee, for this section reads as follows.

18004. Assertion of claims against trust. A claim based on a contract entered into by a trustee in the trustee's representative capacity, on an obligation arising from ownership or control of trust property, or on a tort committed in the course of administration of the trust may be asserted against the trust by proceeding against the trustee in the trustee's representative capacity, whether or not the trustee is personally liable on the claim.

Other Code Sections which have some relevancy to this issue of trustee liability are:

- ◆ California Probate Code Section 15685, which provides that the trustee has an equitable lien on all trust property as against the beneficiary ... for

## APPENDIX “C”

liabilities sustained in the administration of the trust, or because of ownership or control of any trust property, and

- ◆ California Probate Code Section 16011, which basically specifies that the trustee has a duty to take reasonable steps to defend actions that may result in a loss to the trust.

To Summarize the Foregoing:

The trustee is the real party in interest with respect to the trust. Hence, litigation against the trust necessarily involves naming the trustee as a party.

The trustee may be subject to liability for contracts on behalf of the trust.

- ◆ When a contract was entered into before July 1, 1987, unless it is stated in the contract, there is to be no personal liability of the trustee;
- ◆ When a contract is entered into, on or after July 1, 1987, if the contract fails to specify the trust is a party, or the contract fails to reveal the trustee's representative capacity ... cf Zimmer Construction Co v White, 8 Cal. App. 3d 672

Regarding the tort situation, as was set forth in California Probate Code Section 18002; the trustee is generally liable for torts committed by himself, or herself. Probate Code Section 18001 states a trustee can be subjected to liability when he or she is the holder of title to trust property, but only when the trustee is personally at fault for the injury or damages.

A case in California specifies that a trustee who held mere title was not liable for negligence in maintenance of the building where the beneficiary controlled "operation and maintenance of the trust property"; Cf. Richman v Green, 143 Cal App. 2d 470, (1956).

The foregoing is only a brief summary of the various liability provisions in California law regarding the liability of trustees.