Endnote

1. *See* 1839(i)(4) of the Social Security Act defining "modified adjusted gross income" very similarly to the meaning under Internal Revenue Code Section 86. Tax-exempt bond income and the portion of Social Security benefits taxable are subject to an income-related monthly adjustment amount.

TIPS FROM THE PROS

Interesting Trends With Millennials and Trusts

By Al W. King III, co-founder of the South Dakota Trust Company LLC in Sioux Falls, S.D.

Millennials are projected to number 73 million, overtaking Baby Boomers as the largest adult segment of the U.S. population. It's important to note that immigration has assisted with boosting the number of Millennials.[1] Millennials were born between 1981 and 1996 and are ages 25 to 40.[2] They aren't only taking over the workplace but also will soon be taking over the marketplace and could reshape the economy. Millennials generally are looking for innovation, usefulness and experience worth sharing with others and are typically driven by purpose.[3] They spend approximately $600 billion annually in the United States.[4] The younger Generation Z in the United States, ages nine to 24, is the best educated and most diverse generation yet. Many of their thoughts, concerns and opinions are similar to those of the Millennials.[5]

Many existing trusts may not be drafted to best accommodate Millennial beneficiaries and their desires. It may be important to reform/modify or decant these trusts so that their administrative aspects are properly coordinated with not only the desires of the grantor and grantor's spouse but also the Millennial and other beneficiaries. In most instances, traditional trust structures[6] may not be sufficient.

Generally, modern directed trusts[7] are best suited for all generations. The modern directed trust allows a Millennial beneficiary to play a key role regarding both trust distributions and investments. This is extremely important because many Millennials may not share the same views as their parents and grandparents or the trustee.[8] Also, Millennials and other beneficiaries generally have the power to remove and replace a trustee and/or other fiduciary. Initially, this power usually exists with the grantor and the grantor's spouse and on their deaths usually then transitions to a majority of the beneficiaries.[9] This is extremely important because 87% of Millennials replace their parents' advisors.[10] Consequently, understanding the needs and concerns of all the beneficiary generations, such as the Millennials, is important because wealth is always in motion. Approximately $2.3 trillion transitions every two years.[11]

Family Involvement

Millennials are starting families later than their counterparts in other generations. Only 46% of them are married. The share of adults who haven't married is increasing with each generation. It's estimated that approximately 25% of today's young adults won't be married by ages 43 to 53.[12] Many perpetual and long-term trusts are established before any or all of the grandchildren are born. These intergenerational trusts can be established for both existing children and grandchildren as well as unborns. It's estimated that U.S. households will transfer more than $68 trillion in wealth to heirs and charity over the next 25 years.[13] Consequently, intergenerational trusts (for example, dynasty trusts and spousal limited access trusts) are being established at a record pace.

Forty percent of all taxable gifts are being made to irrevocable trusts compared with 12.5% in 1995.[14] The modern directed trusts are the main reason for this increased popularity as a result of their flexibility and control in addition to their ability to involve all generations and their advisors in both trust investment and distribution decisions. Modern directed trusts generally trifurcate the traditional corporate administrative trustee function. There's usually a directed administrative corporate trustee that provides the required trust administrative functions in the directed trust state and takes direction from an investment and/or distribution committee that's typically comprised of family members and family advisors in the family's resident state. Many families prefer this type of structure because they typically have confidence in their own family members and advisors to make proper decisions as fiduciaries for both the trust investments and distributions. Additionally, families can obtain the guidance and oversight of the directed administrative corporate trustee. Consequently, many families desire the directed trust structure.

These modern directed trusts allow for communication with all family members and their advisors. This communication leads to conversations regarding the patriarch's and matriarch's family values as well as those of the adult children. These modern directed trust structures can provide a family with a formula for family governance and education as well as the promotion of family values involving social and fiscal responsibility. They also allow for the understanding of the needs and concerns of the entire family as well as provide a powerful structure to answer those needs and concerns.

Charity

One key need and concern for Millennials is charity. Millennials are leading the way in charitable giving and volunteering. They want to ensure that their donations are impactful and effecting real change.[15] More than 75% of Millennials have made donations to charity, which is more than any other age group. Seventy percent of Millennials believe their parents aren't as committed to charitable giving as they are. Thirty-two percent of them versus 14% of Baby Boomers and the Silent Generation believe that they give back through impact and social investing.[16] Intergenerational family trusts can be structured to allow for impact and social investing to accommodate these Millennial beneficiaries.

Trust Impact/Social Investing

Serving on a directed trust investment committee that's responsible for directing the investment management and monitoring of trust assets can also be a very valuable learning experience for family members.[17] Senior family investment committee members, along with their investment consultants and advisors, can mentor younger family members regarding asset allocation, investment management and the monitoring of both financial and illiquid assets. This opportunity can provide a powerful financial education for young investment committee members and beneficiaries. This is very important to many Millennials.

The Millennial beneficiary, as a member of the investment committee, can direct that a portion of the trust funds be invested to accommodate impact and social justice investing.[18] This could be accomplished by allocating a percent of trust funds for this purpose, establishing separate shares or using an investment management limited liability company (LLC). A Millennial beneficiary can be appointed as the manager of the investment management LLC owned by the trust as the sole member (that is, the owner). The investment committee of a directed trust would generally direct the administrative trustee to hold the investment LLC, which in turn provides the impact and social investment management for the trust.[19]

Furthermore, many families with multiple trusts will sometimes use LLCs and partnerships as the main investment vehicles for their trusts by centralizing investing in the LLCs and/or partnerships and then allocating the units/interests to each trust. This also provides another great way to integrate social and impact investment management to a family trust. Many families often subadvise the investment management for the LLC and or limited partnerships to outside investment managers with specialties in social and impact investing.[20] This strategy also works with common trust funds[21] and business trusts[22] for families with private family trust companies.[23]

Trust Distributions and Charity

Many families realize that family goals aren't the same as philanthropic goals but that successful philanthropy can reinforce family values and, thereby, strengthen a family legacy.[24] Typically, many families accomplish the promotion of social responsibility and successful philanthropy by using private foundations, donor-advised funds, community foundations, pooled income funds, charitable remainder trusts and charitable lead trusts. Personal non-charitable trusts, however, have also become a popular trust vehicle that the wealthy are using to promote social responsibility and successful philanthropy.[25]

The development of charitable giving with non-charitable trusts results from the evolution and popularity of the modern directed trust, which, when combined with active family involvement, has provided a powerful charitable giving alternative. As previously mentioned, the directed administrative trustee in a modern directed trust jurisdiction takes direction from a distribution committee that's usually comprised of family as well as individuals the family is comfortable working with. Most of these trusts are drafted as discretionary trusts. The distribution committee members and their advisors act as mentors for the younger family members on the committee as well as for the beneficiaries. It's recognized that the key time for beneficiary development is generally between ages 20 and 40 (that is, the Millennial's age bracket). In addition to making direct distributions to charities, some families prefer to actively participate in charities. Millennial distribution committee members and beneficiaries generally prefer that distributions be made to charities that focus on causes that they can relate to, and they often volunteer and exhibit other forms of activism.[26]

Some non-charitable trusts have provisions that state that once a trust reaches a certain value, or the beneficiary's net worth attains a certain level, the trust must distribute the excess to a charity either directly or indirectly. This approach ensures that the family gets together to focus on charity and the family's social responsibilities, as well as to actively support the various charitable causes in its community. Other trusts have provisions to supplement a beneficiary's income if they decided to work for a charity, while others match a beneficiary's charitable contribution. Many non-charitable trusts also provide a charitable gift if there are no longer any family beneficiaries. Consequently, providing for discretionary distributions to charity from a non-charitable trust is extremely important to Millennials.[27]

Internal Revenue Code Section 642(c) allows for an unlimited charitable income tax deduction to a non-charitable trust for distributions made from non-charitable trusts to charity. It also shifts the 3.8% net investment income tax to charity. To obtain the IRC Section 642(c) deduction, it's important that the trust have a mandatory direction or a discretionary power to pay funds to charity. Existing trusts can't be reformed/modified to add this power to receive the income tax deduction. The tax advantages are generally secondary with many families, particularly Millennials. Additionally, powers of appointment are also used to appoint funds to charity but aren't always able to accomplish the same goals as discretionary distributions to charity.[28]

Housing

Many Millennials have been hit hard by the Great Recession and have been slower to establish their own households compared with previous generations. Fifteen percent live with their parents.[29] This is nearly double the amount of young Baby Boomers. Approximately 64 million Americans or 20% of the population are in multigenerational households under one roof.[30] This will most likely result in a housing boom in the near future. This housing boom could result in the purchase of homes for Millennial beneficiaries with trust funds. This strategy generally uses an LLC owned by a modern directed trust.[31]

The directed administrative trustee forms an LLC, usually in the same state as the trust situs, though it's not required to be in the same state, and the administrative trustee is also generally the sole member (that is, the owner) of the LLC. A family member or family advisor can generally serve as the LLC's manager; the LLC purchases real estate and pays for related expenses with funds transferred from the trust to the LLC owned by the trust. If the existing trust isn't a directed trust, the grantor can usually reform/modify or decant the trust into a directed trust to best accomplish this strategy.[32]

There are many advantages to purchasing residential real estate within a trust with trust funds for the trust beneficiaries:

- Real estate may remain in the family forever free of estate and generation-skipping transfer taxes.
- Trust beneficiaries may be able to use the residence tax free without paying rent.
- Beneficiaries can generally enjoy use of the home while keeping it protected from divorcing spouses.
- The LLC adds an extra layer of creditor protection.
- If a vacation home, it can be used as a family time share.

These advantages aren't available if parents and grandparents provide family members with down payments outside of the trust to buy a house.[33]

Access Not Ownership

Many Millennials prefer access to products without the burdens of ownership that give rise to what's called a "sharing economy."[34] This applies not only to homes but also to cars, music and other luxury goods.

Purpose trusts are a great way to allow for sharing and the ability to "use" family assets. Purpose trusts don't have any beneficiaries.[35] The sole purpose of such a trust is to care, protect and/or preserve an asset, such as a residence or vacation home, or items such as antiques, cars, jewelry, memorabilia, art, royalties and digital assets. Beneficiaries are allowed to "use" the family property owned by the purpose trust. There's an individual appointed within the trust to enforce the purpose. Additionally, a trust protector and directed administrative trustee are appointed. Most state purpose trust statutes only allow for the care of pets and grave sites. There are a few states, however, that allow for broad and flexible perpetual or long-term purpose trusts. Any legal purpose is generally allowed. Consequently, the purpose trust should gain popularity as a result of Millennials' desires to use and share family properties. Millennials will also welcome the fact that purpose trusts can provide for a philanthropic purpose not otherwise qualifying for a charitable deduction. This could be very important based on their outlooks toward charitable giving and the various causes that they may support.

Technology

Millennials' affinity for technology is also very important.[36] Most Millennials read more in an era of digital content, and this trend affects their desires for products and services. Maximum convenience at a favorable cost is generally desired if their needs and concerns are properly answered. They're used to online price comparisons, product information, peer reviews and other useful information. Consequently, trustees with 24-hour access to trust accounts, combined with other useful direct and indirect technologies, are definite pluses for this group.

Family Wealth Bridge

Americans have accumulated more wealth than any other group in history. They're always in search for the right professionals and the best solutions to assist with the passage of their wealth. Modern directed intergenerational trusts can provide an excellent family wealth bridge between the family patriarchs and matriarchs and their Millennial beneficiary children and grandchildren. Family advisors and trustees will need to carefully and skillfully work with Millennials and other successive generations so that their needs and concerns are properly answered. If this isn't done, it could result in Millennials and other beneficiaries transitioning from their parents' and grandparents' advisors and trustees. This is a powerful and timely opportunity.

Endnotes

1. Kristen Bialik and Richard Fry, "Millennial Life: How Young Adulthood Today Compares With Prior Generations," Pew Research Center (Feb. 14, 2019), *www.pewsocialtrends.org/essay/millennial-life-how-young-adulthood-today-compares-with-prior-generations/.*
2. *Ibid.*
3. David Mizne, "The Millennials Are Coming! The Millennials Are Coming!" *15Five Blog, www.15five.com/blog/the-millennials-are-coming/.*
4. Pamela Bump, "34 Millennial Stats That Marketers Need to Know," *HubSpot* (April 15, 2020), *https://blog.hubspot.com/marketing/millennial-stats/.*
5. *See supra* note 1.
6. The full service, one-stop shopping trustee generally handles custody, taxes, investment management, trust administration and trust accounting. This full trustee service model, although popular in its day, has lost quite a bit of momentum since the mid-1990s with the advent of the modern directed trust and the flexibility and control modern directed trusts provide. *See* Al W. King III, "Drafting Modern Trusts," *Trusts & Estates* (December 2015).
7. Modern directed trust laws provide a family and their advisors with the ability to participate in trust decisions involving investments and distributions. Often, family members and/or close family advisors serve as the investment and distribution committee members. The grantor may also generally serve on the investment committee. Regarding investments, the directed trust provisions allow for either a sophisticated asset diversification model with alternative investments, direct private equity, real estate, etc. or provide the ability to remain entirely liquid with cash. Alternatively, the ability to hold a single position in a public or private security without diversifying is also an option. Additionally, the liability standard for serving on an investment and/or distribution committee is typically gross negligence and/or willful misconduct, thereby providing additional liability protection.
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9. In Revenue Ruling 95-58, for example, the Internal Revenue Service confirmed that a grantor may possess the power to remove a trustee and appoint an individual or corporate successor trustee without being deemed to have retained discretionary control over trust income, provided the grantor doesn't have the power to appoint a successor that's related or subordinate within the meaning of Internal Revenue Code Section 672(c). *See* Al W. King III, "Can a Grantor Have His Cake and Eat It Too?" *Trusts & Estates* (December 2019).
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15. *See supra* note 8; John Roche, "Millennials are Leading the Way in Charitable Giving and Volunteering," *Connecticut Magazine* (Nov. 19, 2020), *www.connecticutmag.com/the-connecticut-story/millennials-are-leading-the-way-in-charitable-giving-and-volunteering/article_d2d13ec2-2903-11eb-9de4-d348d4082f84.html/;* Lawson Bader, "Millennials: How To Cater To The Most Generous Generation," *Forbes* (July 5, 2019), *www.forbes.com/sites/forbesnonprofitcouncil/2019/07/05/millennials-how-to-cater-to-the-most-generous-generation/?sh=7ab66999253a/.*
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17. Al W. King III, "Are Incentive Trusts Gaining Popularity?" *Trusts & Estates* (October 2017).
18. *See supra* note 14.
19. Al W. King III and Pierce H. McDowell, III, "Selecting Modern Trust Structures Based on a Family's Assets," *Trusts & Estates* (August 2017).
20. *Ibid.*
21. A "common trust fund" means a fund maintained by a trustee in which moneys belonging to various estates and trusts in its care are combined for the purpose of facilitating investments.
22. Generally a business trust is a statutory trust established for the purpose of making a profit whereas the trustee(s) administer or manage the capital (for example a business) of the trust for the benefit of the beneficiaries.
23. Al W. King III, "The Private Family Trust Company and Powerful Alternatives," *Trusts & Estates* (February 2016).
24. *See supra* notes 8 and 14.
25. *Ibid.*
26. *Ibid.*
27. *Ibid.*
28. *Ibid.*
29. *See supra* note 1.
30. *Ibid.*
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32. *Ibid.*
33. *Ibid.*
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SPOTLIGHT

Seeing Fuzzy

In Spate, Cricklade by Kurt Jackson sold for $3,140 at Bonhams Modern British and Irish Art auction on Dec. 16, 2020 in London. Equally immersed in art and environmental activism, Jackson's work as Glastonbury Festival's Artist-in-Residence was the subject of a retrospective exhibition last year, in partnership with Greenpeace. Jackson has also worked with many other charitable foundations, including Wateraid, Oxfam and Cornwall Wildlife Trust.

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If you have any questions or would like any additional information, please do not hesitate to call or e-mail us at the numbers and addresses listed below. We also invite you to visit our website at www.sdtrustco.com. We hope to have the opportunity to work with you!

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