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Your Bottom Line

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Navigating a clear course toward your financial security.

Focus on Fiduciary

Warren Mackensen

Since the truth about the activities of money manager Bernard Madoff came to light last December, we have seen a proliferation of stories about fraud or other deceptive practices perpetrated by financial advisors that have hurt their clients. In addition to uncovering a number of Ponzi schemes like Mr. Madoff's, the SEC's recent enforcement actions have highlighted cases involving kickbacks, excessive trading, and misappropriation of funds. It is not a coincidence the apparent increase in the number of these cases has accompanied the market downturn. These illegal behaviors become much easier to detect when account values are falling than when investors are being rewarded by good returns. Had large investors in Mr. Madoff's funds not requested to redeem their shares in response to the market, he might have been able to continue his fraud indefinitely.

These stories are truly discouraging, both for the investing public and professional advisors who act as fiduciaries for their clients. A fiduciary is required by law to act in his or her client's best interest at all times. Clearly, this point was lost on Mr. Madoff. Most consumers of financial advice, however, are not aware that the vast majority of those who call themselves "financial advisors" or "financial planners" are not actually subject to a fiduciary obligation to their clients. Under current rules, advisors who are compensated by third parties on the sale of financial products are subject to a lesser standard known as the "suitability rule." This regulatory hurdle requires only that the product sold be appropriate for the client (in other words, not too risky) at the time of sale. Moreover, this obligation ends once the transaction is completed. The advisor is not required to perform a periodic review to determine if the product purchased is still appropriate.

At Mackensen & Company, we firmly embrace our role as a fiduciary for you. It is part of our culture, not just a regulatory requirement imposed by law. We operate as a fee-only firm in order to fulfill this role, eliminating the conflicts of interest that may arise when advice is delivered through commissioned product sales.

To help educate consumers about the importance of the fiduciary relationship between advisor and client, the National Association of Personal Financial Advisors (NAPFA) hosts a website, www.FocusonFiduciary.com, providing information about the need for a fiduciary standard in the financial services industry as well as a checklist consumers should use in evaluating their own advisor. The NAPFA checklist asks directly whether the advisor is willing to adhere to a fiduciary oath, placing client interests above his or her own and those of his or her employer. This oath, which must be adopted by all NAPFA members, requires that the advisor

- always act in good faith and in the best interests of the client,
- be proactive in disclosing conflicts of interest with the client, and
- not accept any fees or compensation that is contingent upon the purchase or sale of a financial product, or referrals to other professionals.

If your friends and family are not working with a fiduciary advisor, please share this information with them. ❖

FDIC Insurance Limit Increase Extended

David A. Batchelder

As part of the Emergency Economic Stabilization Act of 2008 signed by President Bush in October of last year, the basic limit on federal deposit insurance coverage was increased from $100,000 to $250,000 per depositor. Initially designed as a temporary increase in the coverage limit set to expire at the end of 2009, the $250,000 limit has now been extended until the end of 2013. ❖

Carefully Weigh Options When Naming Trustees . . . .

David T. Mayes

As a tool for passing wealth to your heirs, revocable trusts offer many attractive benefits. Because your assets are owned by the trust when you die, the process of settling your estate becomes relatively simple. There is no need for involvement of the probate court, preserving your privacy and potentially saving time, expenses, and aggravation for your loved ones.

When establishing a trust, one of the most important decisions you make is naming a successor trustee. Typically, you will serve as your own trustee during your lifetime, while you are able. A successor trustee steps in when you can no longer serve due to incapacity. Most often, this successor trustee is a spouse. With people aging into their 90s these days, periods of incapacity are becoming more prevalent, requiring a second successor trustee to step in.

Often, well-intentioned parents name the eldest child as second successor trustee, followed by other children in birth order. While this approach keeps financial management in the family, problems can arise when the child is also a trust beneficiary, or is not well versed in handling accounting, investment and tax matters.

When serving as a trustee, the person you appoint becomes a fiduciary – a person who must set his or her own interests aside when acting for you. Fiduciary responsibility is significant and supersedes any interest the trustee may have in the trust assets after you are gone. Because your interests and those of your beneficiaries are not aligned, this fiduciary duty comes with a conflict for trustees who are also beneficiaries.

Beyond managing this conflict, your child's duties as trustee will include providing an annual accounting to all beneficiaries, filing the various income tax returns and timely distribution of tax schedules to the beneficiaries.

The trustee must also decide how the trust assets are to be invested, a task that may require difficult choices. Again a potential conflict arises because you and your beneficiaries may have competing investment goals – current income for you versus long-term growth for them. Emotional ties can further complicate investment decisions for a child serving as trustee; for example, selling the family homestead after the surviving parent enters a nursing home.

Another difficulty with naming individuals as successor trustees is that there is no guarantee that they will serve. We have seen a situation where two family friends were named as successor trustees. When the trust grantor died, the first served for a short time, then resigned because the job was overwhelming. The backup trustee then declined to serve, requiring court intervention to appoint a viable trustee for their two young daughters.

As an alternative to naming individuals as successor trustees, consider naming a trust company to step in when you and your spouse are no longer able to manage your trust. While this option is often discounted as too impersonal, naming a professional trustee as a backup has several benefits.

First, because a trust company is skilled in trust administration, it is unlikely to make errors in handling required accounting and tax filings.

Second, the trust company will step in immediately when called to serve, eliminating the chance that the courts will have to name a successor if your relative or friend declines the responsibility.

Third, using a trust company eliminates emotional conflicts that can hinder the management of your trust. A professional trustee will be objective in supervising the trust's investment policy and distributions, making sure these decisions are made according to your wishes. Beneficiaries will generally view these independent trustees as evenhanded.

Finally, a trust company offers continuity in managing your investments. If you already have a trusted relationship with a financial advisor, naming a trust company ensures the same people will manage the assets for your children or other beneficiaries.

To discuss including a professional trustee in your estate plan, please contact our office. ❖

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