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Nevada Directed Trusts

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Directed trusts are a relatively modern estate planning tool that allow for the separation of investment management and trustee duties. With a directed trust, the trustee has limited responsibilities, and the grantor can appoint outside advisors to manage investments or direct distributions to beneficiaries. Directed trusts have gained popularity in recent years in estate planning. Nevada has become a go-to state for many individuals and families seeking to establish directed trusts due to its excellent directed trust statutes and other favorable trust laws.

What is a Directed Trust?

A directed trust is a trust structure in which the trustee is directed by one or more designated individuals or entities in making certain decisions related to the trust administration. The person or entity that directs the trustee is called the directing party or directing advisor. Some examples of directing parties include an investment advisor, a distribution committee, or a trust protector. The responsibilities of a directed trustee generally involve the following:

- Carrying out the instructions given by the directing party.
- Maintaining legal ownership of the trust's assets.
- Providing for the preparation of tax returns.
- Maintaining trust records.
- Accounting to the beneficiaries.

The trust document outlines the specific duties and responsibilities of the directed trustee and other trust participants.

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In a directed trust, there are typically at least three distinct roles: the directed trustee, the trust advisor, and the trust beneficiaries. There is also sometimes a trust protector. The trustee administers the trust assets, the trust advisor directs the trustee on certain decisions, and the trust beneficiaries receive the benefits of the trust according to the terms of the trust document.

Choosing the Right State: Why Nevada

Nevada has become a popular state for directed trusts due to its favorable trust laws, including its directed trust

statutes. Nevada statutes permit directed trusts and provide certain protections for directed trustees. One of these protections is that a directed trustee is not held responsible for the actions of the advisor with discretion under the trust agreement, as long as the trustee acts in good faith and does not engage in willful misconduct or gross negligence.

> *"Nevada law offers numerous other benefits for modern trust planning, such as no state income tax, asset protection, and the ability to create perpetual trusts."*

Additionally, the law in Nevada considers a trust advisor to be a fiduciary by default unless the trust instrument specifies otherwise. This means that the trust advisor is legally obligated to act in the best interests of the beneficiaries and to exercise reasonable care, skill, and caution in carrying out his or her duties.

In addition to its directed trust statutes, Nevada law offers numerous other benefits for modern trust planning, such as no state income tax, asset protection, and the ability to create perpetual trusts.

Directed Trust Structures: Different Responsibilities for Different Roles

In a directed trust, various roles can be defined in the trust instrument. One of the key roles is the investment advisor, who is responsible for directing the trustee on investment decisions. The investment advisor can be a financial advisor, a family member, or even the grantor of the trust. Another critical role is the distribution advisor, who directs the trustee on distribution decisions. The distribution advisor can be the same person as the directing advisor or a different individual altogether. It should be noted however, that in most scenarios, the grantor should not act as distribution advisor.

Sometimes, a trust protector may also be appointed to oversee the trustee's actions and ensure the trust's terms are followed correctly. In addition, the trust protector may have other powers defined in the trust, such as removing the trustee and appointing a successor or changing the trust situs.

The roles and responsibilities of each participant are defined in the trust document. Depending on how the trust is drafted, it can be directed for investment, distribution, or both. This means that the directing advisor and distribution advisor can direct the trustee on specific investment choices and distribution decisions, allowing for a more tailored and customized approach to managing and distributing the trust assets.

Modern Trusts: Directed Versus Delegated

Before the inception of the modern-day directed trust, most trusts were drafted the old way: either a single trustee held all powers and responsibilities, or joint trustees shared equal authority and responsibility. The problem with this structure is that trustees, in many cases, were not the best choice for managing the trust assets. At the same time, a manager of a closely held family business or an investment advisor was not fully equipped to undertake all aspects of trust administration. If the trustee lacked the expertise to perform all necessary trustee functions, such as investing trust assets, the trustee's only option was to delegate those duties to a professional equipped to perform the function. The solution to this problem? Update modern trust laws to allow for the separation of trustee duties and responsibilities – hence the modern-day directed trust.

> *"In a directed trust, the advisor has the power to direct the trustee, while in a delegated trust, the trustee is responsible for making investment and distribution decisions."*

The main difference between directed and delegated trusts is the trustee's level of responsibility. In a directed trust, the advisor has the power to direct the trustee, while in a delegated trust, the trustee is responsible for making

investment and distribution decisions. In a delegated trust scenario, the trustee is responsible for all trustee duties, including investment and distribution decisions, and can delegate some or all of those duties to other professionals. However, the trustee remains responsible for ensuring the delegated duties are appropriately executed. In contrast, since a directed trust separates the powers and responsibilities between the trustee and other participants, the trustee responsible for carrying out the directives of the other participants is relieved of liability for complying with those directives, unless the trustee acted in bad faith. This division of responsibilities allows for greater flexibility and customization for trust management.

Solving for Separation of Trustee Duties: "Old and Cold" Trust Documents

What about all the trusts drafted without the flexibility of the directed trust? Plenty of "old and cold" trust documents were drafted before the widespread inception of directed trusts. These trusts do not provide for the separation of trustee duties. As a result, regardless of who controls the trust assets, the trustee remains responsible which often results in difficulty finding a trustee willing to serve with an outside investment advisor who manages the trust assets. In these cases, there are generally three options.

✓ ***Option 1: Decant the Trust to a Directed Trust with Updated Terms or Create a Non-Judicial Settlement Agreement***

Nevada has favorable laws which give trustees the ability to decant a trust to one with updated, modern terms that allow for separation of trustee duties. This will involve the help of a skilled trust attorney familiar with complex trust structures.

Nevada also has a well-established Non-Judicial Settlement process, which allows interested parties in a trust agreement to correct mistakes, address ambiguities, and change administrative provisions without the need for court approval.

✓ ***Option 2: Find a Trustee Who Will Delegate***

Another option, if the terms of a trust do not provide for the separation of trustee duties, is to find a trustee willing to delegate investment management authority to a non-trustee investment advisor. However, because of the increased liability to the trustee under this arrangement, delegated trusts generally incur higher trust administration fees than directed trusts. In addition, under this arrangement, the trustee is required to take on additional monitoring, due diligence, and oversight actions with respect to the investment activities.

✓ ***Option 3: Create an "LLC Wrapper" for Trust Assets to be Managed by Non-Trustee Advisor***

A third option to mitigate risk for the trustee and allow a non-trustee to manage trust assets is to create an LLC and structure ownership so that the only asset at the trust level is an LLC of which the trust is a sole member. In this scenario, the investment advisor or a family member may be appointed as manager of the LLC and will manage the underlying assets held in the LLC.

Summary

Estate planning attorneys should consider using directed trusts because they can be a valuable tool for clients seeking more control over investment and distribution decisions than traditionally structured trusts. Directed trusts have gained popularity in recent years, and Nevada has become a popular state for directed trusts due to its favorable trust laws. Directed trusts offer flexibility and customization for trust management, allowing for tailored investment and distribution decisions. Compared to delegated trusts, where the trustee is responsible for all trustee duties, directed trusts divide powers and responsibilities between the trustee and other participants. However, as always, it is important to carefully consider all aspects of a trust structure and seek the guidance of legal and financial professionals when creating a trust.

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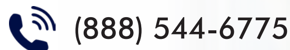

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