MCF Private Trust

HE DID WHAT?!? ETHICS IN THE ESTATE PLAN

The National Malcolm Baldridge Quality Award defines ethical behavior as follows:

"The term, ethical behavior, refers to how an organization ensures that all its decisions, actions, and stakeholder interactions conform to the organization's moral and professional principles. These principles should support all applicable laws and regulations and are the foundation for the organization's culture and values. They define 'right' from 'wrong' behavior."[1]

Ethics is not law. One can do things legally that are unethical. It is just that, a code of behavior that differentiates right from wrong behavior. It is difficult to define exactly and is often a matter of the particular facts and circumstances involved. Nonetheless there are behaviors that are presumptively bad, and most institutions develop policies and procedures to address common circumstances which may arise. This is one of the reasons that working with professionals is a recommended practice. They have been there and done that and should have the ethical compass pre-programmed. Even so, new circumstances arrive and are altered everyday that put people working around large amounts of money in complex arrangements at risk.

Justice Benjamin Cardozo had a real way with words and of the fiduciary role, involved in the role of trustee or executor in the settlement of an estate, he said, "Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior." It is that distinction of behaviors "permissible in the workaday world," being forbidden for fiduciaries that is a subtle distinction with great significance.

It all starts with the creation of the plan. Working with someone who has your best interests at heart, not those who have their own business interests front and center, that can make all the difference. The American Institute of CPAs (AICPA) Code of Professional Conduct calls for an "unswerving commitment to honorable behavior, even at the sacrifice of personal advantage." This opportunity for personal

advantage is one of the most widely observed ethical issues in the estate settlement world, yet most non-professional fiduciaries will dismiss it as "not taking advantage" or "paying a fair price" for the property. Rationalization does not trump ethics. A few examples of unethical behavior in estate settlement may include:

+ The sale of trust property to the fiduciary individually
+ The personal use of trust property
+ The purchase of trust property by fiduciary directly from trust or even at an auction
+ Making a loan from the trust to the fiduciary

This is not to say these things can never be done, but exceptions should follow certain protocols. Exceptions to self dealing transactions can include transactions which are:

+ Authorized in the trust document, although "authorization" does not justify the action by itself, it must also be in the best interests of the beneficiaries
+ Completed with the approval of a court of competent jurisdiction, or
+ Completed with the consent of all of the beneficiaries

When a family member trustee or executor, for example, has a challenge in their home or business finances they may decide to lend themselves money from the estate or trust. They will rationalize that it is good for the estate or trust because I will pay more than the bank will for a CD, however it now puts them in position of both borrower and lender. How would that ever be resolved if things go wrong? Whose interest would they defend, since they are on both sides? The point is that the end result is not the issue, it is that they have put themselves in a position where a conflict of interest exists. That is unethical behavior unless pre-arranged with the exceptions above. It is not always the action itself but the implications that upset the other beneficiaries and sometimes destroys family relationships at the same time. Again, using independent professionals not only assures safeguards through their lack of self interest as both a fiduciary and beneficiary, and double checks through their policies and procedures, and often audit procedures for an internal double check, that unethical behavior is managed ideally to zero.

The duty of impartiality is another important fiduciary standard to ensure there is not only no self-advantage, but also no advantage to one beneficiary over another. Imagine the strain on the relationships for a surviving spouse named as trustee of a trust for which she/he is the current beneficiary and children of the deceased spouse's prior marriage are the remainder beneficiaries, examining every distribution as money not being saved for them. Even with no inappropriate behavior the relationship is often put under great stress, and at a time of strained emotions to start with, the death of a spouse or parent.

Case in point, in the case of Brooke Astor, New York socialite and philanthropist, as her son was named her caretaker, and then, as the New York Times reported, "his life was turned upside down by allegations of mistreatment of his mother and mismanagement of her affairs," a claim initially made by another family member and that led to his conviction at an advanced age followed by time in prison, from which he was released due to failing health. "Well, regrets, naturally" he was quoted as saying, and when asked if he could do it again, would he do things differently he replied, "Quite." And this is the problem. There is no do-over. It is a one-time chance to do things properly. Choose well.

When considering your clients' estate plans, consider not just the competence of the parties they are naming, but the time and the role in which they are being placed. The estate world is full of sad stories of finances, relationships, and lives. As professionals, we too have to follow ethical rules, but at least professionals do not have the built in conflicts as fiduciary and beneficiary, they have done this many times, and have protocols to ensure that ethical issues do not interfere.

[1] "Baldrige Glossary." *Ethical Behavior*, www.baldrige21.com/BALDRIGE_GLOSSARY/BN/Ethical_Behavior.html.

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