Manage Your Business

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Privacy Preferred: Selling a Business Through a Silent Trust

The Key Wealth Institute is a team of highly experienced professionals from across wealth management, dedicated to delivering commentary and financial advice. From strategies to manage your wealth to the latest political and industry news, the Key Wealth Institute provides proactive insights to help grow your wealth.

"But I do not want my children to know we have that kind of money …"

That is a common refrain among business owners planning to transition their financial interests to the next generation. They want to find a balance between preparing the family members for the large concentration of interests they will receive and protecting those interests from being used recklessly.

Creating irrevocable trusts *now* for the benefit of children or charities for tax reasons can be an effective strategy for protecting those assets. A trust allows its creator, or grantor, to take advantage of the current federal transfer tax exemption of $12.06 million (double for married couples filing jointly), shielding future appreciation of assets from income and transfer taxes for generations to come.

Nevertheless, many business owners may not like the idea of providing immediate information to trust beneficiaries. Some fear that knowledge could turn their children or other members of the next generation into stereotypical "trust fund babies," who might deplete the family's financial legacy with profligate spending. Maintaining the confidentiality of trust information from the creditors of beneficiaries, including ex-spouses of children, also can be a logical priority for most business owners.

So what options are available to create trusts for beneficiaries but maintain privacy and confidentiality of trust provisions and assets even from the beneficiaries of the trust?

Creating a silent trust in the handful of states that allow them, like Delaware, may be your best answer.

Beneficiaries' Right to Know

Most states require the grantor to keep beneficiaries reasonably informed of the administration and material facts of the trust. Beneficiary notification is a basic trustee duty as expressed in the Restatement 3rd of Trust Law and comments in The Uniform Trust Code (UTC), which many states have adopted with some modifications.

For instance, if you create a trust funded with closely held business assets for the benefit of your children and grandchildren for creditor protection and estate tax savings in a jurisdiction like New York or California, the trustee must provide adult beneficiaries with notice and information about the trust. Also, for the philanthropic-minded, you can create a charitable remainder unitrust (CRUT) for federal income tax savings and to support your favorite charity, which will receive a lump sum at the end of the trust term. Although the federal income tax savings may be significant, you may not want to disclose the gift to the charity yet, so finding a "silent" solution is paramount.

Silent Trust Solution in Delaware

But even if you live in one of the states that require transparency you can find a "silent" solution in another state that is more flexible.

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Several states have enacted some form of silent trust statute that does not require the trustee to inform trust beneficiaries of the existence of the trust. In 2015, Delaware enacted – and continuously improves via the annual Delaware Trust Act – one of the most robust silent trust laws in the nation.

Establishing a silent trust for tax savings and creditor protection in Delaware can be beneficial for several reasons. Delaware law permits a grantor to create a trust that restricts a beneficiary's right to notice and information of the trust for a period of time, which could be until the grantor's death, the beneficiary reaching a certain age, or a specific date or event. The grantor also can create the position of designated representative to receive notice and trust information on behalf of the beneficiary and represent beneficiaries in any judicial or non-judicial proceeding.

In Delaware, you also can create self-settled asset protection trusts, which allow you to retain a right to receive distributions from the trust and protect the trust's assets from future creditors. These trusts allow for maximum trust investment flexibility by permitting directed trusts – where the grantor or an appointed third party can control the trust's investments.

Despite the silent trust's great utility, circumstances may arise that call for greater transparency regarding trust information but may not require full beneficiary access. Delaware trust law permits modifications of existing trusts, including decanting (pouring some or all of the assets of one trust into the assets of another trust).

An example: You create a trust for the benefit of your children and fund it with your family business assets – some of which are sold for over $10 million. After the sale of a portion of the closely held business assets, the existing silent trust can be decanted to create one or more smaller trusts without notification restrictions. So, the trustee can engage with beneficiaries as it relates to their interests in the smaller trusts but does not have to disclose information related to the larger trust. This is a great way to engage trust beneficiaries while maintaining confidentiality and control over information related to a significant portion of your wealth.

Key Takeaways

Privacy is important to business owners for a myriad of reasons – especially those in the baby boomer generation looking to transition from their business. They may understand the advantages of creating irrevocable trusts for tax minimization and creditor protection purposes. However, many find it difficult to give up control over the flow of confidential legal and financial information related to their closely held businesses held in trusts.

In a world where fewer than 10% of families maintain wealth for more than two generations past the creators of the wealth, it is rational for business owners to want to maintain the integrity and confidentiality of their trust assets. A silent trust is a great option to provide an owner with peace of mind that their family business – often their most prized possession next to their family – or the proceeds of the sale of that business are protected *from* and *for* future generations.

For more information about strategies and ways to plan ahead, contact your relationship manager, or contact our Business Advisory Services team through key.com/businessadvisory.

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