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A Primer About Nominee Realty Trusts

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Nominee realty trusts, a common estate planning device in Massachusetts, are commonly misunderstood and misused. The purpose of this primer is to shed some light on them so they will be better understood and, hopefully, better used.

1. **What is a nominee realty trust?**

A nominee realty trust is a hybrid between a trust and an agency agreement. While they are called "trusts" and have some of the elements of a trust such as a grantor, trustee and beneficiaries, unlike standard trusts, the trustees for the most part act at the direction of the beneficiaries. Typically, trustees of nominee realty trusts hold title to property and can rent it out, collect income, and pay expenses, but cannot sell or mortgage the property unless directed to do so by the beneficiaries.

2. **Why are they used primarily in Massachusetts?**

For many decades, estate planning and real estate attorneys in Massachusetts used nominee realty trusts as a work around for a unique situation in the state. Until 2003, Massachusetts was the only state that required that when property was transferred to trusts that the entire trust be recorded at the registry of deeds. This presented several difficulties. The recording costs could be high due to the number of pages involved. Trusts are often used to keep matters private and can include sensitive details, so most clients would not want their trusts publicly displayed for all to see. And any changes to trusts would require that the amendments or new trustee appointments be recorded at the registry, adding cost and administrative burden. Finally, if someone reviewing title to the property had a question about the terms of a trust, title issues could develop.

To avoid all these potential issues, until 2003 when property was being transferred to trusts, most attorneys recorded nominee realty trusts, simply listing the underlying trust on the schedule of beneficiaries. The schedule of beneficiaries did not have to be recorded (more on this below). Since 2003, Massachusetts law was changed so that now when property is transferred into trust the trustees simply need to record a certificate reciting certain information about the trust, primarily its name and who serves as trustee and successor trustee. As a result, nominee trusts now are used much less frequently than in the past.

3. **What other purposes do they serve?**

While it's no longer necessary to use a nominee realty trust to avoid recording the underlying trust at the registry of deeds, they are still used in some circumstances. They are especially useful when several different people or entities, such as separate trusts or limited liability partnerships, own real estate. Then, rather than listing them all on the deed, they can simply be listed on the schedule of beneficiaries.

This can also avoid difficulties when the beneficiaries may not all agree, cannot be located, become incapacitated, or pass away. In all these circumstances, the nominee realty trust trustees can continue to manage the property. However, they may or may not be able to sell or mortgage the property until the underlying issues are resolved; more on this below.

Nominee realty trusts also facilitate the transfer of ownership interests over time. A parent may want to add their children as owners of a vacation house or a business property, but not be ready to do so all at once. They can give them a small interest at first and add to it over time simply by updating the schedule of beneficiaries. Otherwise, they would have to execute a new deed every time they wanted to change the ownership interests, which would be expensive and cumbersome.

Of course, this type of fractional conveyancing occurred more often when the estate tax threshold was $600,000 and people used the annual gift tax exclusion to make annual gifts and reduce the size of their estates. Now that the federal estate tax threshold is $13.1 million and the Massachusetts one is $2 million, few estates are subject to estate tax in any case.

4. **Why do schedules of beneficiaries go missing so often?**

Schedules of beneficiaries for nominee realty trusts are often misplaced for two main reasons. First, most clients don't understand their importance, so they do not make an extra effort to keep them in a safe place. Second, since nominee trusts are used much less often today than two decades and more ago, most are old. The attorneys who created them may have retired or passed away. And even if they're still practicing, they may not be able to locate the schedules in their files. This also relates to the age of the nominee realty trusts since most were created before attorneys regularly scanned their files.

5. **What can you do about a missing schedule of beneficiaries?**

Where there's agreement about what the original schedule of beneficiaries must have said, the beneficiaries can simply create a new schedule. (Schedules of beneficiaries are typically signed by the beneficiaries, not the trustees.) For instance, if the nominee trust was created at the same time as another trust with the intention of transferring real estate into the underlying trust, it's pretty clear that the schedule of beneficiaries should list the trust. Or if parents created a life estate for themselves with the remainder held by a nominee trust, the family may be certain that the children should be listed on the schedule of beneficiaries.

But what if it's not clear what the grantor intended or there's disagreement? Sometimes matters can be resolved through negotiation or mediation. However, if that's not possible, the only answer may be to go to court. This may be an action to reform the trust or the trustees may seek instructions from the court. In either case, this is most likely to occur in probate court.

Two questions are who has standing to bring an action and who should receive notice. Certainly, the trustee or trustees have standing. The grantor also has standing if they're still alive. If not, their estate should be able to seek guidance from the court.

But what about beneficiaries when the whole problem is that we don't know who the beneficiaries are? The answer is that the court will almost certainly accept an action brought by the next of kin of the grantor and require that such next of kin receive notice of an action brought by the trustees.

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In short, if all interested parties, meaning the next of kin of the grantor, agree, they can simply create a new schedule of beneficiaries. But if they don't, they'll have to seek a court resolution.

6. **What powers do the trustees have?**

Typically, nominee realty trusts provide that the trustees can manage property, rent it out, pay taxes and other expenses, and hold title. However, they cannot sell or mortgage the property unless directed to do so by the beneficiaries.

7. **What happens if the beneficiaries disagree?**

Most nominee realty trusts simply state that the trustees must act at the direction of the beneficiaries. If the beneficiaries disagree, matters related to the sale or mortgaging of property will be unable to move forward. Ultimately, if the parties can't come to agreement, they may need to seek court intervention. The trustees might seek instructions from the court or a beneficiary might seek to sell the property through a partition action.

To avoid this happening, our firm has revised the standard nominee realty trust to say that trustees will act the direction of those beneficiaries holding a majority interest in the trust. This way, no single owner can prevent actions which everyone else wants. If, for instance, there are four equal owners, three can direct the sale or mortgaging of property. If there are five, still three can act since together they will have a 60 percent interest.

8. **What happens if the trustees act without the necessary instructions?**

While the trustees must only take major actions like selling or mortgaging property as directed by the beneficiaries (whether by all or by a majority as provided in the trust instrument), third parties normally do not communicate with the beneficiaries. They act based on the assurance of the trustees that they have the necessary authority and they may rely on that assurance.

So, for instance, if the trustees sell real estate owned by the nominee realty trust without receiving the required instructions from the beneficiaries, the sale still stands. But the objecting beneficiary or beneficiaries may be able to sue the trustees for damages. (Of course, the damages may be little or nothing if the sale was appropriate and for fair market value.)

9. **What happens when a beneficiary dies?**

If the schedule of beneficiaries lists a beneficiary in their individual name, if they pass away, their interest will pass to their estate. Their estate will have to be probated. If they have a will, their interest will pass as directed in their will. If not, it will pass through the rules of intestacy, essentially to their closest relatives.

If the ownership interest was held by a trust, the terms of the trust will determine what happens to the beneficiary's interest after they die. In most cases, no probate will be necessary.

We have seen schedules of beneficiaries that attempt to avoid probate by stating what happens upon the owner's death. For instance, the schedule might say that the parents are the beneficiaries during their lives and after they have passed away their interest passes to their

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children. Or the schedule might say that all the owners are joint with rights of survivorship, so if any single owner dies, their interest passes to the surviving owners. In practice, these schemes seem to work. As long as everyone agrees on the results, and the trustees are comfortable acting as directed by the new beneficiaries, there's no problem.

On the other hand, as a legal matter these schedules can be problematic. First, they're often not written clearly. The trust says that the trustees must act as directed by the beneficiaries. Then if the schedule says the parents have a life interest with the remainder passing to their children, must the trustees receive instruction from all members of the family? In other words, what is meant by "beneficiary?" It's often not well defined.

Further, such schedules muddy the water on whether a nominee realty trust is an agency agreement or a trust. If the beneficiaries are not clear or can change over time, for whom do the trustees act as agents? It's much cleaner to use a trust as beneficiary when the grantor wants to set out the succession of ownership interests.

10. Who fills out the schedule of beneficiaries?

Typically, the beneficiaries sign the schedule of beneficiaries and the trustees sign an acknowledgement that they have received the schedule. We have seen schedules signed by the trustees and not the beneficiaries, but this is not a good practice. The agent has too much power if they declare on whose behalf they are acting. The actual owners should, instead, appoint the trustees who are acting as their agents.

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