What Is a Trust?

Thinking about formation of trust so you must understand the legal framework and Legal requirements, benefits and challenges.A trust deed outlines the terms and conditions governing the establishment and management of a trust. It is important to understand the legal framework before you decide to form a trust where the property being transferred into the trust, and understand the roles and responsibilities of the trustee's executor. Your rights and objective of the trust must be protected. Trust deed is an essential document for the proper functioning and administration of a trust. A trust is a fiduciary relationship where a trustor grants another party, known as the trustee, the right to hold title to property or assets for the benefit of a third party

Parties in a Trust

- Author/Settlor/Trustor/Donor: The person who wants to transfer his property and reposes confidence on another for the creation of the trust.
- Trustee: The person who accepts the confidence for the creation of the trust
- Beneficiary: The person who will benefit from the trust in the near future.

Types of Trusts

1.Private and Public Trusts:

A private trust is for a closed group. In other words, the beneficiaries can be identified. E.g.: A trust created for the relatives and friends of the author.

A public trust is created for a large group, i.e. the public in large. Eg: Non-Profit NGO's Charitable Institutions for the general public.

2. Living or Testamentary Trusts:

A living trust, also called an inter-vivos trust, is a written document in which an individual's assets are provided as a trust for the individual's use and benefit during their lifetime. A trustee is named when the trust is established; this person is in charge of handling the affairs of the trust and transferring the assets to the beneficiaries at the time of the grantor's death.

A testamentary trust, also called a will trust, specifies how an individual's assets are designated after the grantor's death. It is not established until after the grantor passes away.

3. Revocable or Irrevocable Trusts

A revocable trust can be changed or terminated by the trustor during that person's lifetime.

An irrevocable trust, as the name implies, cannot be changed once it's established.

4. Funded or Unfunded Trusts

A funded trust has assets put into it by the trustor during their lifetime.

An unfunded trust consists only of the trust agreement with no funding.

Laws governing Trusts in India

The Indian Trust Act, 1882 ('Act') governs the private trusts established in India. This Act is applicable to the whole of India.Public trusts in India are usually governed by state-specific legislation, such as The Maharashtra Public Trust Act, 1950.

Purposes of Trusts

Trust maybe crated for any purpose which is lawful.As per Section 4, all purposes are said to be lawful unless it:

- Is forbidden by law
- Defeats the provisions of law
- Is fraudulent
- Involves injury to another person or his property
- Immoral or against to public policy

Why establish a trust?

You can have confidence that your assets will be safeguarded and dispersed in accordance with your preferences by using a trust to arrange your estate. Although creating a trust can be more

costly and time-consuming than creating a will, there are a number of possible advantages to trusts, such as:

· avoiding probate and distributing your assets more quickly and easily.

· Giving you more flexibility and control by giving precise instructions on who gets your assets and how (e.g., distributed over time, at someone else's choice, etc.).

· reducing conflict since, unlike wills, trust instructions cannot be challenged in court.

· preserving your privacy by preventing the probate process's public record of your assets.

· defending possessions from litigation and creditors.

· Reducing taxes, ascertain types of trusts can reduce estate, gift or income taxes.

Who can create a Trust?

A trust may be created by:

- Every person who is competent to enter into contracts: This includes an individual, AOP, HUF, company, etc.
- If a trust is to be created by on or behalf of a minor, then the permission of a Principal Civil Court of original jurisdiction is required.

Creation of Trust

The act defines how the author could create the trust, assign trustees and give them his monetary assets to be controlled by the trust. It may be express or implied. It includes-

- Intention of the author to create the trust.
- Purpose of the trust.
- The monetary asset is assigned for the benefit of the trustee.
- Gives control or transfer the trust property to the trustee which includes intention of the author.
- Trustee can claim expenses & salary from the benefits from the trust of his work.

Procedure to form a Trust

1. Name of the Trust

The trust's name must first be decided upon by the participants. The trust's name cannot violate any laws, including the Intellectual Property Rights Act, the Trademarks Act, or the Copyrights Act. Furthermore, the trust's name cannot violate the 1950 Emblems and Names Act.

2. Settlers of the Trust

The trust's settlers must be chosen by the parties. Aside from this, the number of trustees that must be taken into account has no upper limit. For a trust to be established, a minimum of two trustees are required. The author is unable to

serve as a trustee for the trust, nevertheless. An additional prerequisite is that the trustee must be an Indian resident.

3. Form Memorandum of Association for the Trust-

The company's Memorandum of Association outlines the purposes for which the trust was established. A corresponding memorandum of association (MOA) exists for the trust. This covers the trust's goals and the purpose for which it was established. The trust is only necessary to carry out legal objects.

4. Draft the Trust Deed

One acceptable document for creating a trust is a trust deed. When a trust is established between parties, the trust deed needs to be presented to the companies' registrar. The following must be considered when creating the trust deed:

- Trust name.
- Where the trust has its registered office or place of business.
- Which activities are carried out by the trust?
- What are the objectives of the trust? Whether they fall in place with the legitimate objects of the business.
- Information related to the authors/ trustors and trustees.
- What are the net assets owned by the trust? Are there any other assets owned by the trust?
- Information related to the board of directors of the trust. Any other information on the shareholders and directors of the trust
- Qualifications, the quorum of the board, and other information regarding the trust.
- Duties and responsibilities of the board of directors, managers, and other members of the trust.
- Powers and Functions of the Managing Trustees and other members of the trust.
- Any other information about the trust and the amendment of the trust.

5. Submit the deed to the Registrar

The drafted deed needs to be sent to the registrar. The parties who will draft the deed are as follows. The recipient, the trustee, and the writer. The trust deed would contain all of the relevant terms and conditions. The trust deed functions similarly to a company's articles of association. It includes all of the trust's bylaws as well as other pertinent information. The requirements of the law stipulate that it must be on stamp paper. The amount owed on the stamp paper needs to match the value of the property.

6. Obtain Certificate of Trust Registration

The trust will be registered once the registrar reviews all the documents and determines that everything is in order. The certificate of trust registration will be given by the registrar. Both the trustee and the trustor are required to retain this certificate of trust registration. Following this, the corresponding bank account can be opened.

Documents Required

- 2A and 80 G Certificate from the respective income tax authorities to claim any form of deductions
- Trust Deed with the respective stamp value.
- Two Photographs of the parties in the trust.
- PAN Card of the individuals having a trust.
- Address Proof of the Individuals.
- Identity Proof of the Individuals.
- Authentication from the Partners.
- No Objection Certificate for using the Premises
- Any form of Utility Bill.
- Address Proof of the Registered Office of the Trust

What is a family trust?

The term “family trust” describes any trust that benefits the grantor’s family members.The purpose of a family trust is to protect and manage family wealth, ensuring its smooth transfer and preservation across generations. By placing assets into a trust, the settlor gives up direct ownership but can retain control over how those assets are utilized and distributed as trustee. The beneficiaries of the trust can receive income generated by the trust's assets or even have access to the assets (Corpus) themselves, subject to the terms set by the settlor.

Laws governing Family Trusts in India

The Indian Trust Act, 1882 governs all the laws related to formation, operations and dissolution of Family Trusts in India.

What are advantages and disadvantages of a Family Trust?

Advantages:

- no hassle/delay/cost of obtaining Probate
- Protection/preservation of Assets/wealth
- no risk of any family objection for distribution
- control/management of property given to trusted persons for Life Care of Special Child, Minors, ageing Parents, Business management
- Avoid forced heirship/community property laws
- Tax saving tool

Disadvantages:

- Managing separate accounting of Trust income and filing of tax returns
- Tax rates – maximum marginal rate

Legal issues in Family Trusts

1. Difficult to amend

Many trust deeds lack provisions for amendments, causing them to be powerless to adapt to changing circumstances. Amendments are crucial in situations like changes in beneficiary circumstances or shifts in tax and regulatory regimes. However, if a trust deed lacks an amendment clause or contains an overly restrictive one, trustees may transgress their authority and engage in actions not specifically authorized by the deed, potentially leading to decisions being contested by beneficiaries.

The Indian Trusts Act, 1882 prescribes that trustees must apply to a civil court for their opinion, advice, or direction for the management or administration of the trust-property. In such cases, trustees can file a civil suit for rectification of the trust instrument if the real intention of the parties is not expressed in the trust deed[1].Civil suits can succeed if trustees and beneficiaries consent to proposed trust deed amendments, and external parties are not likely to be adversely impacted by the changes[2].

Families must decide whether to submit the trust documents to the court or collapse the existing structure and adopt a fresh one. In cases where families have established a public charitable trust, the process of amendment can be multi-layered, with the consent of the Charity Commissioner being a prerequisite. As a public trust structure has a wide beneficiary base, it is essential for trustees to seek legal opinion and guidance in such matters.

2. Modifying how the trust's assets are managed

Trust management practices need to be updated to cater to the changing needs of high net-worth families who are increasingly looking into alternative asset classes and geographical diversification. Antiquated trust deeds often lack clear provisions and restrict investment options, making it difficult for trustees to make sophisticated decisions regarding the trust corpus. To address this issue, trust deeds should be updated to include specific language regarding the allocation of funds and income for various purposes. This will ensure that the trust remains relevant and efficiently utilized for the benefit of its stakeholders. By recalibrating management practices, trustees can better navigate the complexities of modern investments and effectively grow the trust corpus.

3. Non-resident trustees

The Indian Trusts Act allows non-resident trustees to be appointed as trustees, but this right is often not exercised by beneficiaries. Section 60 of the Act allows beneficiaries to demand that trust assets are managed by "proper" trustees, which does not include those permanently outside India or domiciled abroad. If trustees are absent for six months or leave India to live abroad, a new trustee may be appointed. However, this right is often not exercised by beneficiaries and can be weaponized if stakeholder relationships become incompatible. To mitigate risks, the trust deed should expressly permit non-resident trustees to hold the office of a trustee.

4. Restrictions under Indian foreign exchange control regulations

The Indian foreign exchange control regulations (FEMA) do not explicitly prohibit or restrict transactions related to private family trusts involving non-resident family members. However, the Reserve Bank of India (RBI) has clarified that what is not permissible directly under the regulations should not be undertaken indirectly through a private trust structure. FEMA imposes various restrictions regarding the transfer or gift of funds or assets to non-residents, as well as repatriation of cash or proceeds on sale of such assets by non-residents. However, timeworn trust deeds may provide for transfers that are inconsistent with the extant restrictions. In such cases, trustees and beneficiaries may find themselves in a quandary as to how to proceed. Some strategies may include establishing separate structures for non-resident family members

or amending the timelines for distribution or revising the allocation matrix for assets and income streams between resident and non-resident beneficiaries.

5. Validity of the arbitration clause in trust deeds

Trust disputes can arise due to various factors, including ambiguous provisions, conflicting interests, inefficient trust management, or breach of fiduciary obligations by trustees. Arbitration clauses were traditionally included in trust deeds, but a 2016 Supreme Court ruling[3] rendered arbitration clauses redundant. Beneficiaries are not signatories to the trust deed, making arbitration clauses redundant. Therefore, any disputes arising from the trust deed must be decided by a competent court of law. Families should consider incorporating alternate dispute resolution mechanisms into their trust deeds, such as internal or external mediation with a predefined panel of family well-wishers and professionals. This would prevent disputing parties from resorting to civil court proceedings.

How to safeguard family trust documents?

· Store in a safe

Store the documents in a home safe that is waterproof and fireproof. To make it simple for you and your loved ones to access them, you can use a digital combination with a backup key.

· Draft and review the trust document.

Create and go over the trust agreement. Get a lawyer to draft the trust agreement, then go over it with them to make sure your wishes are reflected correctly. The terms and conditions, such as the beneficiary distribution schedule, the kinds of assets held in the trust, and the trustee's authority, should be included in the document.

· Transfer assets into the trust

Place all assets in the trustee's name, including money and real estate titles.

· Specify conditions

Conditions that initiate the addition or deletion of a beneficiary can be specified. For instance, you can stipulate that a beneficiary forfeits any trust assets or income in the event of a divorce.

· Include details of guardians

For any minor beneficiaries, you can provide information about the guardians who will oversee their finances.

- Registration of Trust Deed

Non-testamentary instrument needs to be signed by the author of the trust or the trustee and has to be registered to safeguard from any legal intricacies.

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[1]Commissioner of Income Tax, Kanpur v Kamla Town Trust [(1996) 7 SCC 349]

[2]Muffakham Jah Bahadur v HEH Nawab Mir (AIR 1989 AP 68)

[3]Vimal Kishor Shah v Jayesh Dinesh Shah [(2016) 8 SCC 788]

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