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Squabbling for Dollars

Family trusts are a common, but volatile, commercial real estate-owning entity

BY JULIE NAKASHIMA
CREJ Staff Writer

With interest rates low and new laws offering plentiful enticements, the commercial real estate industry's mom and pop operation — the family trust — is seeing unusually active purchasing levels this year.

Families that own property together are eagerly "trading up," according to Martin Cohan, a broker in the Los Angeles office of Grubb & Ellis who deals primarily with family trusts, and has managed more than 100 transactions for them over the past 15 years. Cohan, along with Joshua Levy of Grubb & Ellis, recently represented family trust buyers in the purchases of a 14,000-square-foot retail center in Las Vegas; Campus Pointe, a 137,000-square-foot retail center in San Diego; and La Paz Office Plaza, a seven-building, 180,000-square-foot office complex in Laguna Hills.

Changes in estate tax laws and the rising popularity of 1031 exchanges are offering family trusts new ways to shelter their investments from taxes, and new impetus to buy.

Yet as commercial real estate owners and managers, family trusts are highly volatile, subject to the same divisive forces that afflict families themselves. These include death — the primary reason for having a trust in the first place — divorce and, to put it politely, family members' pecuniary ambitions.

Close to the Vest

If there is any one trait that characterizes family trusts as buyers, it's that they make conservative, low-leveraged investors, Cohan said.

"They have equity. They want to protect that equity, and they want a return on that equity," he said.

His clients even include some developers, who are "past their risk-taking days," as Cohan put it.

"They took their risk when they were younger, and they don't want to risk their family fortunes by taking a lot of risk [now]," he said. "They're conservative, but savvy."

Anybody who is married with children, who cares where their assets are going and who doesn't want the expense of probate is a candidate for a family trust, said attorney Michelle C. Lerman, who prefers the term living trust.

The partner in San Rafael-based Lerman & Lerman, puts trusts together and occasionally takes them apart or "revokes" them — one of the chief reasons being divorce.

"If your assets are greater than the exemption amount, then you should consider a living trust," Lerman said, referring to the amount people can leave to their heirs without paying estate taxes.

"The typical family trust is created by Mom and Dad," said William O. Passo, a real estate attorney whose Santa Ana-based investment firm, Passco Real Estate Enterprises, sees family trusts involved in about half of its transactions.

During the parents' lives, the trust is revocable and they generally act as the trustees. Upon their deaths, the assets go into one or more "pots," one for each child. But even the best-laid plans can go awry.

"The interesting experiences are when children, who are beneficiaries of the trust, want to get their parents to give them money earlier, so they try to challenge the provisions of the trust," Passo said, adding that scenario is more likely to happen after one parent has died.

Other times, Mom and Dad make it into their 80s, "and the kids are in their 60s and they're saying, 'How long do we have to wait?' They want to get their money now."

In most cases, Cohan said, "the impetus of the transaction was that the guy who created great wealth for the family felt it was time to switch horses, sell small and buy big, or do something to either build or further secure his assets."

Bypass the Bickering

If a family is prone to bicker over money or other issues, having a trust really won't amplify that problem, Passo said. On the other hand, a trust does nothing to lessen that tendency.

"The issues tend to be the same. If mom and dad die and they've got multiple kids, and they name one of the kids as trustee, then that can cause hostility among the children," Passo said. "But if mom and dad don't have a trust, you can still have hostility: 'I want the ring,' 'I want the coat,' 'I want the whatever.'"

It's not uncommon for the nontrustee beneficiaries to be unhappy with decisions that the trustee makes, and cause instability for the



Attorneys Jeffrey Lerman, left, and Michelle C. Lerman say anyone who is married with children, who cares where their assets are going and who doesn't want the expense of probate, is a candidate for a living trust.

CREJ STAFF PHOTO BY S. TODD ROBERTS

trust, Passo added. For instance, they'll accuse the trustee of creating unnecessary fees and skimming them off the top before the rest of the estate gets divided, or selling properties too cheaply, or hiring a particular broker and getting some sort of compensation or kickback.

"The number of allegations that can occur are only limited by the imagination," Passo said. "In some cases, they resort to litigation, and certainly families have broken up over how the estate got divided."

But, he pointed out, you can have that problem with a will, too.

"You can end up having will contests. There's absolutely hundreds of cases in the law journals dealing with this kind of family dispute," Passo said.

But then, that's not all that different from other types of real estate owning entities.

"Even if two major institutions go in together on a property," Cohan said, "they may find themselves with different goals at a certain point in time, and can't resolve it with communications, and they end up in court with one another."

Family trusts are, in effect family businesses, much like any other business partnership, he observed. The difference, he said, is that some members find themselves in the partnership by "default."

"They didn't buy into it," Cohan said. "They just found themselves as a member of this partnership, because their father put it together."