

# CURRENT TRENDS AND SPECIFICS REGARDING CHANGES IN FIDUCIARY LAWS AND STANDARDS

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# History & Overview

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- Harvard vs. Amory – 1800's Massachusetts Case establishing the Prudent Man Theory
- Uniform Prudent Investor Act – 1994
  - ◆ Adopted by 41 States and DC and Virgin Islands
- Uniform Principal & Income Act – 1997
  - ◆ Adopted by 46 States and DC
  - ◆ Under Section 104, added a "Power to Adjust", and by Section 105, a protection for trustees for the adjustment decision
    - This precipitated the "Unitrust Conversion" options in many states
  - ◆ Previous Uniform Acts in 1931 and 1962

# History & Overview

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- Statement of the Law of Trusts
- Restatement of the Law of Trusts 2<sup>nd</sup> and 3<sup>rd</sup>
  - ◆ From the American Law Institute
- Uniform Trust Code 2000
  - ◆ Adopted by 24 States and DC
  - ◆ To create consistency in law, and clearly, to reduce fiduciary risk through the time constraints placed on beneficiaries for seeking redress
  - ◆ Full text available at: [www.uniformlaws.org](http://www.uniformlaws.org)

# Uniform Trust Code

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- 11 Articles:
  - ◆ **Articles 1** and **11** deal with definitions and rules of statutory interpretation, as general provisions
  - ◆ **Article 9** has no content, but allows inclusion of the Uniform Prudent Investor Act, if a state wants it as part of the whole

# Uniform Trust Code

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- **Article 2** – Judicial Proceedings
- **Article 3** – Representation
- **Article 4** – Creation, Validity, Modification, and Termination of a Trust
- **Article 5** – Creditor's Claims; Spendthrift and Discretionary Trusts

# Uniform Trust Code

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- **Article 6** – Revocable Trusts
- **Article 7** – Office of Trustee
- **Article 8** – Duties and Powers of a Trustee
- **Article 10** – Liability of Trustees and Rights of Persons Dealing with Trustees

# Section 105

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- Default and Mandatory Rules
  - ◆ Terms of the Trust prevail, *except*:
    1. The requirements to create a trust
    2. The duty of a trustee to act in good faith, in accordance with the terms and purposes of the trust and the interests of the beneficiaries
    3. The requirement that a trust and its terms be for the benefit of its beneficiaries, and that the trust have a lawful purpose, not contrary to public policy, and possible to achieve

# Section 105

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- Default and Mandatory Rules

- ◆ Terms of the Trust prevail, *except*:

4. The power of the court to modify or terminate a trust under sections 410-416
5. The effect of a spendthrift provision and the rights of certain creditors and assignees to reach a trust as provided in Article 5
6. The power of the court under Section 702 to require, dispense with, or modify or terminate a bond



# Section 105

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- Default and Mandatory Rules

- ◆ Terms of the Trust prevail, *except*:

7. The power of the court under Section 708(b) to adjust a trustee's compensation specified in the terms of the trust which is unreasonably high or low
8. The duty under section 813(b)(2) and (3) to notify qualified beneficiaries of an irrevocable trust who have attained 25 years of age of the existence of the trust, of the identity of the trustee, and of their right to request trustee's reports

# Section 105

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- Default and Mandatory Rules

- ◆ Terms of the Trust prevail, *except*:

9. The duty under Section 813(a) to respond to the request of a qualified beneficiary of an irrevocable trust for trustee's reports and other information reasonably related to the administration of a trust
10. The effect of the exculpatory term under Section 1008

# Section 105

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- Default and Mandatory Rules
  - ◆ Terms of the Trust prevail, *except*:
    11. The rights under Section 1010 – 1013 of a person other than a trustee or beneficiary
    12. Periods of limitation for commencing a judicial proceeding

# Section 105

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- Default and Mandatory Rules

- ◆ Terms of the Trust prevail, *except*:

13. The power of the court to take such action and exercise such jurisdiction as may be necessary in the interest of justice
14. The subject-matter jurisdiction of the court and venue for commencing a proceeding as provided in Section 203 (identification of the selected court) and 204 (the venue of the court to situs of trustee, or when trusteeship is vacant, to situs of the beneficiary)

# Article 4

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- Creation, Validity, Modification, and Termination of a Trust
  - ◆ Trust Requirements: Intent, Corpus, Trustee, Beneficiary(s)
    - Allows for “Honorary Trusts”, as for animals or other non-charitable purpose – an innovation not generally allowed under the common law
    - Not required to be “in writing”

# Section 411

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- Describes the circumstances under which an irrevocable, noncharitable trust can be modified or terminated:
  - ◆ May be compelled by beneficiaries, with or without settlor concurrence
  - ◆ Without settlor concurrence, the court must find that continuance of the trust is not necessary to achieve any material purpose of the trust
  - ◆ A spendthrift provision is not considered necessary to constitute a material provision of the trust
  - ◆ Assets to be divided by beneficiary agreement
  - ◆ When not all beneficiaries consent, the court must find that if all had consented, the change could have occurred; and the interests of the non-consenting will be adequately protected

# Section 412

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- This section broadens the court's ability to apply equitable deviation to terminate or modify a trust, as much as possible within the intent of the settlor
- Changing economic or capacity issues are the types of changes that might be considered

# Article 5

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- Spendthrift provisions in a trust protect those assets until distribution to the beneficiary occurs.
- A beneficiary who owes child support, spousal maintenance, or a creditor for services provided to protect the beneficiary's interest in the trust cannot rely on the spendthrift provision



# Article 5

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- Additionally, a spendthrift clause may also not protect against a claim of the enacting state or the United States to the extent state or federal law so provides
- Under UTC, self-settled trusts would not have creditor protection while they remain revocable
- Fiduciary “discretion” can, of course, be subject to judicial review

# Article 7

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- Office of the Trustee
  - ◆ Acceptance of the trust by the trustee
  - ◆ Bond for the trustee
  - ◆ Decision-making by co-trustee
  - ◆ Compensation of the trustee
    - Standard is “reasonable compensation”
    - Court may review and change

# Article 7

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- ◆ Removal of trustee
  - Settlor, co-trustee, beneficiary, or court may request:
    - ◆ Breach of trust
    - ◆ Lack of cooperation among co-trustees
    - ◆ Defects in trustee where removal is in the best interest of beneficiary(ies)
    - ◆ Change of circumstances

# Section 704

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- Vacancies in **noncharitable trusteeship** must be filled when *no* trustee exists:
  - ◆ 1) By a person/entity named by the document
  - ◆ 2) By a person/entity unanimously selected by the qualified beneficiary(ies)
  - ◆ 3) By a person/entity selected by the court

# Section 704

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- Vacancies in **charitable trusteeship** must be filled when *no* trustee exists:
  - ◆ 1) By a person/entity named by the document
  - ◆ 2) By a person/entity selected by the charitable organization designated to receive distributions
  - ◆ 3) By a person/entity appointed by the court
- The court may always add a trustee or special fiduciary, as deemed necessary

# Section 706

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- Removal of Trustee:
  - ◆ The settlor, a co-trustee, or beneficiary may petition for removal of a trustee
  - ◆ A trustee may be removed by the court on its own initiative for cause:
    - Serious breach of trust
    - Lack of cooperation among co-trustees
    - Unfitness, unwillingness, persistent failure to administer effectively

# Section 706

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- Contrary to common law, the ability of a settlor to petition for removal of a trustee is unique in the UTC
- However, it does *not* allow any other rights, such as reports, or administrative information

# Article 8

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- Duties and Powers of the Trustee:
  - ◆ Liability is the primary duty
  - ◆ Other standard duties are articulated, except those of the Uniform Prudent Investor Act
  - ◆ Includes the duty to keep beneficiaries informed, BUT with some very new twists...



# Section 813

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- Fundamental duty to keep beneficiaries reasonably informed, so they are able to protect their own interests applied to “qualified beneficiaries”:
  - ◆ A copy of the trust on request
  - ◆ Information within 60 days of trustee acceptance; or irrevocable status of trust
  - ◆ Advance notice of compensation change

# Section 813

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- Requirements apply *only* to prospective trusts, following the enactment of the UTC; or those that become irrevocable after the enactment date

# Article 10

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- Liability of Trustees and Rights of Persons Dealing with the Trustee provides remedies when there is a breach of trust, who and when there is an action available by anybody, and trustee immunity from *personal* liability
- Available damages and invoking the court's powers of equity to compel performance

# Section 1005

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- Limitation of Action Against Trustee
- Section 1005(a) restrains a beneficiary from commencing a proceeding for breach of trust more than 1 year after the date the beneficiary or their representative was sent an adequately disclosed report disclosing the existence of a potential claim

# Section 1005

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- Without the referenced (a) notification, a breach will be barred if not commenced with 5 years after the first to occur:
  - ◆ 1) Removal, resignation, or death of the trustee
  - ◆ 2) Termination of the beneficiary's interest
  - ◆ 3) Termination of the trust

# Section 1006

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- Reliance on the Trust Instrument
  - ◆ *Reasonable* reliance on the terms of the trust, as expressed in the instrument, ensures a trustee is not liable to a beneficiary for a breach

# Specifics to Illinois

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- Though Illinois has not yet accepted the UTC, there are some changes for us as well. Both of the following were signed on 8-10-2012 and are effective 1-1-2013, as amendments to the Trust and Trustees Act of Illinois:
  - Illinois enacts Directed Trust Statute as HB 4663
    - ◆ Protects Trustees from acting or not acting pursuant to the directions of a directing party, generally “investment trust advisors”, “trust protectors”, and/or “distribution trust advisors”
    - ◆ The Trustee may be treated as an “excluded fiduciary” with no liability to the beneficiaries where the roles and responsibilities are separated completely.

# Specifics to Illinois

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- Illinois enacts Decanting Statute as HB 4662
  - ◆ Grants Trustees of certain trusts, a discretionary power to appoint the principal of one trust to the trustee of a second trust. Applies to all trusts under Illinois law unless specifically prohibited.
  - ◆ When the original Trustee has absolute power to distribute, the new trust can favor one, some, or all beneficiaries in the new trust.
  - ◆ However, when that power to distribute is limited, the second trust must provide both current and successor beneficiaries who are the same, including any distribution standards and beneficiary powers.



# Specifics to Illinois

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- The Decanting does not require beneficiary, grantor, or court approval; so long as notice of the intention is given to current and presumptive remainder beneficiaries and there are no objections given within 60 days.
- There are further provisions concerning Supplemental Needs Trusts for special needs individuals, the continued application of the Rule Against Perpetuities applicable to the first trust, and certain tax limitations.
- The Illinois Attorney General's Charitable Trust Bureau must be given notice if there is any charitable beneficiary

# Impending Changes at the Federal Level - Trust

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- Dodd-Frank
  - ◆ NO EXCEPTION for anyone from registration with SEC has impact for family office operations. Must register with SEC or form a Trust Company.
  - ◆ Concerns with Hedging, Commodities, and Futures
    - Commodity Futures Trading Commission (CFTC) will supervise and monitor
    - This is a work in progress
- Consumer Financial Protection Bureau (CFPB)
  - ◆ Currently focused fairly exclusively on Lending
  - ◆ Not likely to be involved with Trust, but no promises...

# Impending Changes at the Federal Level - Trust

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- Universal Fiduciary Standard
  - ◆ Questions exist for Registered Investment Advisors (RIA), currently deemed to have a fiduciary standard versus Brokers, who currently operate under a Suitability Standard
- FTC would like to push this out to ALL WEALTH...
- Scenario with Trust is based not on SEC or FTC, but rather through regulation of State Regulators and/or Federal Reserve; or the Office of the Comptroller of the Currency (OCC)
  - ◆ Trust also has a very long history in Federal and State Law; and always developing Case Law