COMMITTEE REPORT:
ESTATE LITIGATION

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Progressive or Regressive?

Some contrarian questions about new-fangled trust codes

Every now and then, in an area as complex as trusts and estates, it behooves even experienced lawyers to view things afresh. From 30,000 feet, we can ask frank, or even contrarian, questions to help deepen our understanding of our field as it is and as it might evolve.

What do we mean by contrarian questions? Well, if we consider recent alterations to state trust codes, what's the direction of change? What drives the change? What long-established principles are weakening? Who gains and who loses? How will the various interests react? And as disputes inevitably arise, how will courts respond?

Here are several recent "progressive" trends in trust codes and what we hope are challenging questions.

Minimizing Fiduciary Accountability

When it comes to trustee liability, how little is too little?

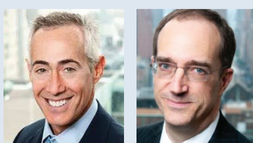
One might think that a floor was established—and a strong signal sent—in 2000 by the Uniform Trust Code (UTC). Section 1008 of the UTC suggests that an exculpation clause should be unenforceable to the extent that it "relieves the trustee of liability for breach of trust committed in bad faith or with reckless indifference to the purposes of the trust or the interests of the beneficiaries."[1] The *Restatement (Third) of Trusts (Restatement Third)* language is similar, if a bit less favorable to trustees: An exculpatory clause is enforceable:

> except to the extent that it purports to relieve the trustee (a) of liability for a breach of trust committed in bad faith or with indifference to the fiduciary duties of the trustee, the terms or purposes of the trust, or the interests of the beneficiaries, or (b) of accountability for profits derived from a breach of trust.[2]

Despite such suggested uniform standards, progressive trust jurisdictions appear to be racing to the bottom, treating the UTC almost as a ceiling, rather than a floor. Updates to statutory trust codes, subsequent to the UTC, have treated fiduciaries even more generously, including by further minimizing a fiduciary's duty to account and streamlining a fiduciary's ability to be released from liability for its actions.

In 2011, Nevada enacted a terms-of-trust provision that allows broad exculpation. Under that statute, a trust instrument may vary the "standard of care" for a fiduciary, other than by exculpating "willful misconduct or gross negligence."[3] To drive the point home, the legislature directed, "This section must be liberally construed to give maximum effect to the principle of freedom of disposition and to the enforceability of trust instruments."[4]

Other provisions don't depend on the trust instrument. In 2007, Florida changed its law to provide that if a trustee satisfies certain standards of disclosure and notice, then the trustee may benefit from a statute of limitations of only six months for a claim for breach of fiduciary duty.[5] That special 6-month period for trustees is far shorter than the typical 4-year period that applies to fiduciary duty claims generally.[6]



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The Tennessee Trust Code creates a 1-year limitations period that begins to run when the beneficiary (or trust advisor, trust protector or a representative) is "sent information that adequately disclosed facts indicating the existence of a potential claim for breach of trust."[7] The information sent is adequate if it's "sufficient" to cause the recipient "to be presumed to know of the potential claim or to know that an additional inquiry is necessary."[8] The 2013 comments to Tennessee's Section 1005 acknowledge that in some ways it differs significantly from the UTC and the *Restatement Third.* Indeed, the UTC would provide for one year after a "report" (not merely information that discloses facts).[9]

The appeal of these duty- or liability-limiting provisions for trust companies, trust administrators and those who serve as trustees is obvious. But why might settlors opt for states where accountability is decreasing?

In most areas of the law, we think that the prospect of liability for misconduct results in performance that's improved. So shouldn't settlors want their beneficiaries to be protected from trustee misfeasance or malfeasance? Are settlors succumbing to the blandishments of trust administration marketing? Or does a family's entrepreneurial generation favor flexibility, as opposed to supervision and enforcement? Do settlors regard trustee accountability as an expense to be avoided? Does that affect decision making when settlors choose jurisdictions?

And from 30,000 feet, where and when will the fiduciary exculpation trend stop? If everything but the worst bad faith and malfeasance is absolved, then controls will be relatively weak. Indeed, that appears to be the point of exculpatory clauses—to make onerous fiduciary duties lighter and less expensive to trusts. But with lower standards and less control, errors will be made, both by trustees and courts. Perhaps the public won't be up in arms when trust beneficiaries lack remedies. But will the industry—much less legislatures and courts—be satisfied when egregious cases arise and are litigated, and no accountability results?

In considering these questions, an analogy is in order. We see now in trust law what happened a century ago in corporate law. New Jersey began to lure corporations away from New York—and then Delaware lured them away from New Jersey. Delaware offered corporations a degree of flexibility that made it the leading state in which to organize. That flexibility has its proponents among corporate lawyers and executives (though shareholder activists might disagree). Delaware corporate law is very sophisticated, and the Court of Chancery may be the world's leading business court.

Is that corporate governance dynamic one that the law of trusts should re-enact? Should any state become the Delaware of trust law?[10]

Share ownership is a choice. If an investor doesn't prefer the Delaware regime, then that regime may be avoided. Don't buy shares in Delaware corporations.

Should trust law also account for the interests of beneficiaries—many under age or as yet unborn—who can't speak for themselves?

Trusts, however, are different. To be sure, any intergenerational trust is a gift. And in establishing it, settlors and trustees contract. They'll do so only on terms that they find satisfactory, and to the extent they can, they'll choose favorable law. But should trust law also account for the interests of beneficiaries—many under age or as yet unborn—who can't speak for themselves?

This is particularly true now that, in some jurisdictions, trusts may extend over many lifetimes. (See "Dynasty Trusts," below.) It may make good sense for the wishes of a settlor to prevail over the presumptive preferences of a later generation or two. But when beneficiaries increasingly number in the hundreds or thousands—and they will, with trusts that last for 365 years, 1,000 years or in perpetuity—then courts might begin to wonder. Several centuries hence, when the interests of many

beneficiaries are at stake, the written wishes of one settlor, unknown to anyone living, will be given less weight.

Courts deciding business disputes today don't ask what the CEO who founded the company in 1879 would have wanted. Will the law of trusts, asking that question, seek to answer it with any force? Should it?

Directed Trusts

Another example of laws being tailored to settlors' current interests is the directed trust. Here, states—often following the 2017 Uniform Directed Trust Act—are allowing fiduciary powers and duties to be unbundled. Typically, a directed trust enables the settlor to distribute administrative duties to a trustee in a progressive state, with less onerous administration and lower fees, and at the same time, to allocate investment-management duties elsewhere. The allure appears to be to economize on administration while enabling assets to be managed by a home state, longstanding advisor or specialist who's familiar with the settlor's values and can be counted on to manage the assets as the settlor would want.

> Are beneficiaries best served by bifurcations or trifurcations of fiduciary powers?

Such arrangements make sense for trusts that require specialized knowledge, perhaps involving unique assets. A trust corpus that includes major works of art may require the expertise of a gallerist. A trust that contains a family business may need advice from someone familiar with that industry. In these ways and others, the ever-increasing flexibility afforded by directed trusts has proven quite appealing to settlors.

But are beneficiaries best served by such bifurcations or trifurcations? Nevada's directed trust provisions allow for various roles including custodial account owner, directing trust advisor, distribution trust advisor, investment trust advisor and trust protector.[11] Such divided responsibilities can mean unclear authority, poor communication and "after-you-Alphonse" inaction. Complex arrangements also make monitoring more complicated. As duties are sliced and diced in subtle ways, unsophisticated beneficiaries may wonder who's truly minding the store—and whom to hold to account when things go wrong.

Here, note how the South Dakota statute allows for divided responsibilities. Both the "investment trust advisor" and the "distribution trust advisor" may exercise powers in their sole discretion, with decisions binding on other fiduciaries; for both roles, the standard is the "best interests of the trust."[12] Best interests, however, is a malleable standard, and different advisors will have different views.

Alaska in 2013 amended its trust advisor statute to provide that if a trustee is required by the trust instrument to follow the direction of a trust advisor, then the trustee is absolved of liability, "regardless of the information available to the trustee."[13] Moreover, such a trustee doesn't have any "obligation to review, inquire, investigate, or make recommendations or evaluations," in exercising a trustee power, if that exercise complies with the directions given.[14]

Here too, the long term must be considered. A century hence, no one living will have any first-hand knowledge of the settlor's wishes or values. No one will have spoken to the settlor in decades. And the industry in which the settlor made money might not even exist. The original bifurcation of administration and management may seem pointless and arbitrary—or even unwise—if a fiduciary or advisor takes a settlor's wishes, recorded in writing long ago, too far.

Silent Trusts

A further unbundling of fiduciary duties is reflected in the silent trust, now allowed by statute in certain states, including Alaska, Delaware, Nevada and South Dakota. In Nevada, a statutory change in 2015 allows a settlor to:

> restrict, eliminate or otherwise vary the rights and interests of beneficiaries in any manner that is not illegal or against public policy, including . . . The right to be informed of the beneficiary's interest for a period of time.[15]

A recent revision to South Dakota's Trust Code goes further: there, a settlor (or trustor) may eliminate the beneficiary's right to be informed of the existence of the trust "for a period of time" or even—new in 2023—"indefinitely."[16]

Compared to a traditional structure, what's effectively unbundled isn't the fiduciary, but the beneficiary.

By definition, a silent trust has a beneficiary who doesn't know that the trust even exists. In some jurisdictions, the settlor may designate a representative of the beneficiary to receive the information that the fiduciary would typically impart directly to the beneficiary. Conceptually, this approach involves designating an alternative beneficiary of the trustee's obligations to disclose material information—part of the fiduciary duty of candor.[17]

This arrangement may give rise to a further fiduciary relationship between the designated representative and the beneficiary. Again, complexity is introduced that may disfavor beneficiaries. Moreover, will a representative protect a beneficiary's interests as actively as the beneficiary?

The usual rationale for a silent trust is the worthy goal that the settlor wants to instill thrift in the next generation and seeks to keep the very knowledge of wealth from the persons to whom it will eventually be transferred. On that view, perhaps statutory age limits should be the rule (despite South Dakota's "indefinitely" language)?

Of course, some beneficiaries are financially incompetent at any age. For them, however, silent trusts perhaps aren't the appropriate remedy. Their needs may be well served by a simple trust providing a certain amount of money per year, indexed to inflation, for a beneficiary whom the settlor perceives to be permanently unable to handle great wealth.

Dynasty Trusts

In a further progressive move, over the past 40 years, many states have extended trusts' permissible durations. In 1987, Nevada allowed interests to vest or terminate within 365 years, and in 2015, the Nevada Supreme Court held that the statute didn't violate a constitutional provision that might have been thought to invalidate it.[18] Not to be outdone, in 1995, Delaware allowed certain trusts to have perpetual duration.[19] Effective July 1, 2022, Florida now allows trusts to last for 1,000 years.[20]

For centuries, the common law didn't allow trusts of these durations. Presumably—if we think, along with some learned judges and scholars of law and economics, that the common law arrived at efficient outcomes[21]—such long-term trusts had a downside that, it was thought, should be avoided. What was the public evil that the rule against perpetuities sought to avert?

As to real property, the undesirable result was restraints on alienation that could exclude land from commerce and development for extended periods of time.

But that couldn't have been the social rationale behind restrictions on durations of trusts that invested in financial instruments. And even if it were historically the rationale as to land in England, what should be the rule as to all forms of property in the United States?

> By changing trust codes, states may also be causing social and political changes whose consequences can't be anticipated and whose ultimate effects can't be known.

Here we pose perhaps our most contrarian questions of all. Is dynastic formation something that American law should encourage? Weren't dynasties something that immigrants to America thought they were leaving behind? If we think the United States is a land of economic opportunity and social mobility, then why should wealth be tied up for centuries, or even forever, in certain families? Might dynasty trust statutes give rise to a trust aristocracy? Would that accord with our vision of America? And should the law of trusts and estates be the engine to work this change?

Looking Ahead

If these sound like social or political questions—they are. By changing trust codes, states may also be causing social and political changes whose consequences can't be anticipated and whose ultimate effects can't be known.

And this brings us to a final, larger point. Many progressive trust jurisdictions are advertised as politically stable. Conscientious trust companies, of course, point out that tax laws can change. But some actors also point to certain constitutional provisions, as if to suggest that a state's current law can't or won't change.

That's a fallacy. Rather, among the current incongruities is the fact that some of the most trust-flexible states have lively—indeed, *progressive*—political histories. If we look back a century or more, South Dakota was a hotbed of prairie populism. If we look ahead a century or more—as 365-year-or-longer trusts suggest we must—how can we have any confidence that current statutory or constitutional arrangements will persist?

In advising settlors, estate-planning lawyers counsel clients about what to do with their assets. As the parties who own the resources at issue, settlors look to attorneys, politicians and jurisdictions that will maximize their flexibility in life and their ability to control their hard-earned money, even from the grave.

So we understand why the pendulum is now swinging as it is. But we also wonder whether someday there might be a reaction. Trusts-and-estates law now offers a new form of immortality to the wealthy. How will the rest of society respond?

When the revolution comes to Sioux Falls, don't say we didn't ask questions.

Endnotes

1. Uniform Trust Code (UTC) Section 1008(a)(1).
2. *Restatement (Third) of Trusts* Section 96(1). Such language has its limits. In 2015, interpreting a similar statute, the Supreme Court of Nebraska held that it didn't exculpate a trustee from, among other things, "providing a false address to insurers" and failing to inform the beneficiaries that insurance premiums hadn't been paid and that the policies had lapsed. *Rafert* v. *Meyer*, 290 Neb. 219, 228 (2015).
3. Nev. Rev. Stat. 163.004(3)(a).
4. *Ibid.*, at 163.004(4).
5. Fla. Stat. Ann. Section 736.1008.
6. *See* Fla. Stat. Ann. Section 95.11(3); *compare also* Fla. Stat. Ann. Section 95.11(4)(a) (providing 2-year period for actions "founded on negligence").
7. Tenn. Code Ann. Section 35-15-1005(a)(1).
8. *Ibid.*, Section 35-15-1005(b).
9. UTC Section 1005.
10. Our colleagues in the Delaware trusts-and-estates bar probably think that Delaware is already the Delaware of trust law.
11. Nev. Rev. Stat. 163.553–557.
12. S.D. Codified Laws Sections 55-1B-10 and 55-1B-11.
13. Alaska Stat. Ann. Section 13.36.375
14. *Ibid.* So far, *Westlaw* suggests, this Alaska provision has been litigated only once. Is that a sign of efficiency or an indication of overcomplexity?
15. Nev. Rev. Stat. Section 163.004.
16. S.D. Codified Laws Section 55-2-13(3).
17. *See, e.g.*, *McNeil* v. *Bennett*, 792 A.2d 190, 211 (Del. Ch. 2001) (Strine, V.C.) (finding "overwhelming evidence" that trustees had breached fiduciary duty by failing to inform adult beneficiary of his status "for *several decades*") (italics in original), *aff'd in part, rev'd in part sub nom. McNeil* v. *McNeil*, 798 A.2d 503, 510 (Del. 2002) (affirming as to failure to inform because, "even in the absence of a request for information, a trustee must communicate essential facts, such as the existence of the basic terms of the trust. That a person is a current beneficiary of a trust is indeed an essential fact.").
18. *Bullion Monarch Mining, Inc. v. Barrick Goldstrike Mines, Inc.*, 131 Nev. 99, 102 (2015) (construing Nev. Rev. Stat. Section 111.1031).
19. 25 Del. C. Section 503.
20. Fla. Stat. Ann. Section 689.225.
21. *E.g.*, Richard Posner, *Economic Analysis of Law* 27 (Aspen 5th ed. 1998) (describing "efficiency theory of the common law"—that "many areas of the common law, especially but not only the great common law fields of property, torts, crimes, and contracts, bear the stamp of economic reasoning"). On the rule against perpetuities specifically, Posner argues that "arrangements for the distant future [are] likely to result in an inefficient use of resources brought about by unforeseen contingencies." *Ibid.*, at p. 560.