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DRAFTING THE UNIFORM TRUST ACT

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The Uniform Trust Act is the first comprehensive attempt at the national level to codify the law of trusts. This paper describes the reasons for the Act, its current status, and many of its provisions. Comments are welcome and may be sent to the author at the University of Missouri School of Law, 203 Hulston Hall, Columbia, MO 65211 (englishda@missouri.edu). The current draft, dated October 13, 1999, is available at website - www.law.upenn.edu/bll/ulc/ulc.htm.

GENERAL BACKGROUND

1. What is the current status of the Uniform Trust Act?

Before a uniform act is officially approved, it must be "read" at least twice by the Uniform Law Commissioners at its annual meeting. The Uniform Trust Act had its first reading at the Commissioners' 1998 annual meeting, and its second reading this year. The Act is expected to be finally approved by the Commissioners in July, 2000. The drafting of the Act has been a multi-year project. The Trust Act drafting committee was appointed in 1994, and serious drafting began in 1995.

2. Who is participating in the drafting process?

The Act is officially drafted by a committee consisting of Uniform Law Commissioners, who are appointed by the governors or legislatures of their respective states. The function of the Reporter is to carry out the drafting committee's decisions on a day-to-day level and to prepare the drafts for each meeting. The committee is assisted by numerous advisors and observers, representing an array of organizations, who sit in and participate at drafting sessions. One of the principal tasks since the project began has been to contact as many groups as possible to ensure that all interested groups are represented and have the chance to provide input.

3. What trust law models are the drafting committee consulting?

While the Uniform Trust Act is the first comprehensive *uniform* act on the subject of trusts, comprehensive trust statutes are already in effect in several states. Notable examples include California, Georgia, Indiana, Missouri, and Texas. Most influential has been the 1986 California statute, found at Division 9 of the California Probate Code (Sections 15000 *et seq*.), which was used by the drafting committee as its initial model. The California law also draws heavily from the other state models. The California law was only a starting point, however. The draft at this point is entirely the drafting committee's work product. Since drafting began in 1995, each of the California provisions has been discussed by the drafting committee and either accepted, rejected or revised. The provisions which remain have also been reorganized. In the process, the trust statutes of all other states have been reviewed.

4. When can states begin considering the Act?

While there will doubtless be additional revisions before the Act is finally completed, states may begin considering the Act now. It is not uncommon for states to enact uniform acts prior to or in tandem with approval at the national level. The comments of state and local bar associations studying a preliminary draft of a uniform act are quite valuable and are often incorporated into the final version. The Act is already under consideration in several states. In fact, earlier this year Iowa became the first jurisdiction to enact the Act.

5. Why is a Uniform Trust Act being drafted?

There are several reasons why the drafting of a Uniform Trust Act is timely. The primary stimulus for the drafting of the Act is the much greater use of the trust in recent years, both in family estate planning and in commercial transactions, both in the United States and internationally. This greater use of the trust, and consequent rise in the number of day-to-day questions involving trusts, has led to a recognition that the trust law in many States is quite thin. It has also led to a recognition that the existing uniform acts relating to trusts, while numerous, are incomplete. The primary source of trust law in most States is thus the Restatement (Second) of Trusts and the multivolume treatises by Scott and Bogert, sources which fail to address numerous practical issues and which on others sometimes provide conflicting guidance. The Uniform Trust Act hopefully will provide precise answers to these questions and in an easily findable place, providing the basis for an efficient system which is fair to both trustees and beneficiaries.

6. Aren't there already numerous uniform acts on trust law subjects?

There are numerous uniform acts on trusts and related subjects, but none provide comprehensive coverage of trust law issues. Certain of these smaller acts are incorporated into the larger Uniform Trust Act. Others, addressing more

specialized topics, will continue to be available for enactment in free-standing form. The following is a list of some of these other acts:

Uniform Trustee Powers Act - approved in 1964, it has been enacted in 16 states. The Act, as its name implies, contains a long list of specific trustee powers and addresses selected other issues, particularly relations of the trustee with persons other than beneficiaries. The Trustee Powers Act is badly outdated and is entirely superseded by the Uniform Trust Act, principally at Sections 816 and 1012. States enacting the Uniform Trust Act should repeal this other uniform act.

Uniform Prudent Investor Act - approved in 1994, this act has already been enacted in over 30 states. This Act, and variant forms enacted in a number of other States, has displaced the older prudent man" standard, bringing trust law into line with modern investment practice. States which have enacted the Uniform Prudent Investor Act are encouraged to recodify it as part of this Act. A place for this is provided in Article 9.

Uniform Principal and Income Act - a major revision of this widely enacted uniform act was approved in 1997. The Act extensively revises the accounting rules applicable to both trusts and estates. Because the Principal and Income Act, both in its current and prior versions, covers accounting for both estates and trusts, a jurisdiction enacting the Uniform Trust Act may wish to codify its principal and income law either as part of this Act or as part of its probate code.

Uniform Management of Institutional Funds Act - approved in 1972, this Act has been enacted in 46 jurisdictions. This Act governs the administration of endowment funds held by charitable, religious, and other eleemosynary institutions. The Act establishes a standard for prudence for using appreciation on assets, provides specific authority for the making of investments and delegating this authority, and specifies a procedure, either through donor consent or court approval, for removing restrictions on the use of donated funds.

Uniform Custodial Trust Act - approved in 1987, this Act has been enacted to date in 15 jurisdictions. This Act, which allows standard trust provisions to be automatically incorporated into the terms of the trust simply by referring to the Act, is not displaced by the Uniform Trust Act but complements it.

Uniform Probate Code Article VII - approved in 1969, Article VII has been enacted in about 15 jurisdictions. Article VII, though titled "Trust Administration," is a modest statute, addressing only a limited number of topics, including trust registration, jurisdiction, and trustee liability to persons other than beneficiaries. The substance of Article VII, other than its provisions on trust registration, are absorbed into the Uniform Trust Act, its provisions on jurisdiction at Article 2, and its provision on trustee liability to persons other than beneficiaries at Section 1011.

Uniform Common Trust Fund Act - approved in 1938, this act has been enacted in 34 states. The drafters of the Uniform Trust Act have elected not to address the subject of common trust funds and will leave this other act undisturbed. In recent years, many banks have replaced their common trust funds with proprietary mutual funds that may also be made available to non-trust customers. The Uniform Trust Act addresses the use of such proprietary funds at Section 802.

Uniform Trusts Act (1937) - this largely overlooked Act of the same name was enacted in only six states, none within the past several decades. Despite a title suggesting comprehensive coverage of the subject, this Act, like Article VII of the UPC, addresses only a limited number of topics. These include the duty of loyalty, the registration and voting of securities, and trustee liability to persons other than beneficiaries. States enacting the current Uniform Trust Act should repeal this earlier namesake.

Uniform Supervision of Trustees for Charitable Purposes Act - approved in 1954, this Act has been enacted in four states. This Act is limited to mechanisms for monitoring the actions of charitable trustees and does not address the substantive law of charitable trusts, including the doctrine of cy pres. Cy pres is addressed in Section 408 of the Uniform Trust Act.

Uniform Testamentary Additions to Trusts Act - this Act comes in two versions: the 1960 Act, with 31 enactments; and the 1991 version, with 16 enactments through 1997. This Act validates pourover devises to trusts. While not incorporated into the Uniform Trust Act, the Testamentary Additions to Trusts Act, like the Uniform Trust Act, is designed to facilitate the use of the revocable living trust.

Uniform Probate Code - approved in 1969, and enacted in close to complete form in about 20 States but influential in all, the UPC overlaps with trust topics in several areas. One area of overlap, already mentioned, is UPC Article VII. Another area of overlap concerns representation of beneficiaries. UPC Section 1-403 provides principles of representation for achieving binding judicial settlements of matters involving both trusts and estates. The Uniform Trust Act adopts these representation principles, and extends them to nonjudicial settlements concerning trusts and to required and optional notices and consents. See Uniform Trust Act, Sections 109 and 203, and Article 3. A final area of overlap between the UPC and trust law topics concerns rules of construction. The UPC, in Article II, Part 7, extends rules on the construction of wills to trusts and other nonprobate instruments. The Uniform Trust Act similarly extends to trusts the rules on the construction of wills. However, unlike the UPC, the Trust Act does not prescribe the exact rules. Instead, Section 110 extends to trusts whatever rules on the construction of wills the enacting jurisdiction already has in place.

7. How does the drafting of the Uniform Trust Act relate to the Restatement of Trusts?

The Restatement (Second) of Trusts was approved by the American Law Institute in 1957. Beginning in the late 1980s, work on the Restatement Third began. The portion of Restatement Third relating to the prudent investor rule and other investment topics was completed and approved in 1992. A tentative draft of the portion of Restatement Third relating to the rules on the creation and validity of trusts was approved in 1996, and the portions relating to the office of trustee, trust purposes, spendthrift provisions and the rights of creditors was approved in May, 1999. The Uniform Trust Act is being drafted in close coordination with the writing of the Restatement Third

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ANALYSIS OF DRAFT

The following is a summary of the current draft with a focus on the key issues which have arisen in the drafting process.

Article 1
General Provisions and Definitions

Section I02. Definitions

Among the more important definitions are the definitions of "property," "qualified beneficiary," "settlor," "terms of a trust," and "trust."

The requirement of property is one of the basic elements of a trust. The property used to initially fund a revocable trust is often insubstantial, however. The definition of "property" (paragraph (11)) makes clear that something as insubstantial as a revocable designation of beneficiary is a sufficient property interest to activate the trust and the duties of the trustee.

Many trust instruments provide that certain actions may be taken upon notice to or with the consent of less than all of

the beneficiaries. For example, a trust typically allows a trustee to resign upon notice to the beneficiaries currently receiving or eligible to receive the trust income. The definition of "qualified beneficiary" (paragraph (12)) codifies this common drafting technique, except that the class of beneficiaries is expanded to include not only the income beneficiaries but also the first-line remaindermen. The result is that certain actions, including a trustee resignation (Section 705), the appointment of a new trustee in the event of a vacancy (Section 704), and notice of the trustee's annual report (Section 813) may be accomplished without the consent of the holders of remote remainder interests.

The definition of "settlor" (paragraph (14)) provides quite simply that a settlor means a person who creates an inter vivos or testamentary trust. But this simplicity, as the comment to the section makes clear, may mask what is sometimes a difficult determination whenever more than one person is involved. For example, what if the grandparents later make annual exclusion transfers to an irrevocable trust for a grandchild which was initially created and funded by the child's mother? Are all three of them settlors or only the mother? Or what if the parent makes an annual exclusion transfer to a child's revocable trust? Does that parent become a settlor with respect to the contribution?

The definition answers at least some of these questions. To the extent an individual makes a contribution to a trust over which someone else holds a power of revocation, that person is not a settlor. Otherwise, if it is concluded that a trust does in fact have multiple settlors, the definition treats each person as a settlor to the extent of that person's proportionate contribution. Determining the identity of the "settlor" is important, among other things, for determining rights to revoke (see Section 602) and the statute of limitations on possible contest (see Section 605).

The definition of "terms of a trust" (paragraph (17)) leaves open the possibility that the settlor's oral statements and conduct, to the extent admissible in a judicial proceeding, may be taken into account in determining meaning. A trustee, however, is protected from liability for reasonably relying on the terms of a written trust instrument (see Section 1007).

The definition of "trust" (paragraph (18)) is key to determining the scope of the Act. The definition includes only express trusts, thereby automatically excluding both resulting and constructive trusts, which are remedial devices implied by law. The definition also includes a trust created by court decree which is to be administered in the manner of an express trust, such as a trust created to hold a personal injury settlement. The definition does not specifically exclude trusts created for commercial purposes, such as trusts to hold retirement benefits, but the Act, as its contents make clear, is directed primarily at trusts related to the donative transfer of property.

Section 103. Mandatory Rules

This section first clarifies that the Act is primarily a default statute. A settlor is generally free to vary the trustee duties and powers prescribed by the Act. This section next lists the limits on this ability. A settlor may not vary the requirements for creating a trust or certain of the provisions relating to termination and modification. A settlor may not limit the ability of the court to intervene as necessary in the interests of justice, and may not negate the obligation of a trustee to act in good faith and in accordance with fiduciary principles. A settlor may not eliminate the trustee's duty to keep the beneficiaries reasonably informed of the trust's administration, or limit the protections afforded persons other than beneficiaries in their dealings with trustees.

Section 105. Common Law of Trusts

This provision, providing that the Act is supplemented by the common law, may appear to state the obvious, but it actually goes to the heart of the Act. How many topics should the Act attempt to tackle? This provision recognizes that it would be a mistake to try to codify everything and that the Act should instead focus on those issues most amenable to codification.

Section 106. Choice of Law

This provision extends to trusts a couple of provisions derived from the UPC. Subsection (a), derived in part from UPC Section 2-506, validates the creation of a trust not created by will if the trust was created in compliance with the law of a state in which the settlor had a significant contact. Trusts created by wills are excluded because the creation of wills is addressed by other law.

Subsection (b), copied in part from UPC Section 2-703, permits the settlor to select the law to control the meaning and effect of the trust's terms. The law selected by the settlor will control despite the geographic situs of the trust property. In accordance with traditional doctrine, a choice of law provision cannot override a significant public policy of the forum jurisdiction. In the absence of a choice of law provision, the Act adopts the standard from the Restatement (Second) of

jurisdiction. In the absence of a choice of law provision, the Act adopts the standard from the Restatement (Second) of Conflict of Laws - the meaning and effect of the terms of the trust are to be determined by the law of the state most significantly related to the issue in question.

Section 107. Principal Place of Administration

This section deals with selected aspects of the principal place of administration. With the administration of a trust occurring in some instance in several jurisdictions simultaneously, or even in cyberspace, the Act does not attempt the probably impossible task of comprehensively stating how to determine a trust's principal locus. To reduce possible uncertainty on this point, a settlor should consider designating the principal place of administration in the terms of the trust. This section validates such a choice if the trustee's principal place of business is located in or a trustee is a resident of the designated place, or if all or part of the administration occurs there.

Changing a trust's principal place of administration is sometimes desirable, particularly to lower a trust's state income tax. Other reasons may include the relocation of the trustee or beneficiaries, the appointment of a new trustee, or a change in the location of the trust investments. Many trust instruments deal expressly with this issue, but for those which do not, this section provides a procedure for transferring the principal place of administration to another State or country. Prior to moving the trust, the trustee must give at least 60 days advance notice to the qualified beneficiaries. While court approval of a transfer is not required, the court does retain authority to order, approve, or disapprove a transfer.

Section 108. Trust Registration.

This section, which is based on comparable provisions of the Uniform Probate Code, grants a trustee the *option* to register the trust in the place of principal administration. Registration permits the locus of the trust to be better affixed and may facilitate transactions with third parties. Jurisdiction continues in the place of registration until released by joint consent of the trustee and all of the qualified beneficiaries.

Section 109. Nonjudicial Settlement Agreements

To encourage resolution of disputes without resort to the courts, this section clarifies the circumstances when a binding out of court settlement can be obtained. In particular, only such matters as a court could properly approve may be made the subject of a nonjudicial settlement. For example, a nonjudicial settlement may not be used to validate an action that would otherwise be illegal, such as to terminate a trust in a manner not authorized by the Act. To give a nonjudicial settlement binding effect on minor beneficiaries and others who cannot participate in the agreement, it will frequently be necessary to use the representation procedures of Article 3.

Section 110. Rules of Construction.

This section extends to trusts whatever rules the enacting jurisdiction has on the construction of wills. The extension is not automatic but extends only such rules as the court determines pertinent. Because of the great variety of approaches taken in the states on the construction of wills, the drafters concluded that it would be a mistake to prescribe the particular rules for the construction of trusts. Rather, the better policy is that the rules for trusts in general should be the same as the state's rules for wills, whatever those rules might be.

Article 2
Judicial Proceedings

This article addresses selected issues involving judicial proceedings concerning trusts, particularly trusts with contacts with more than one State or country. This article is not intended to provide comprehensive coverage of court jurisdiction or procedure with respect to trusts. Many such issues are better addressed elsewhere, such as in the state's rules of civil procedure or as provided by court rule.

The jurisdiction of the court is available as invoked by interested persons or otherwise exercised as provided by law, although commencement of a judicial proceeding involving a trust need not result in continuing court supervision (Section 201). The trustee and beneficiaries, by operation of law, are deemed to have consented to the jurisdiction of the court at the principal place of administration as to any matter relating to the trust (Section 202). Section 203 specifies the persons who must be notified of a judicial settlement in order to bind a beneficiary represented under Article 3. Sections 204 and 205 are optional, bracketed provisions relating to subject-matter jurisdiction and venue.

Article 3
Representation

This article deals with representation of beneficiaries, both representation by fiduciaries (personal representatives, guardians and conservators), and what is known as virtual representation. Virtual representation is a doctrine that allows binding representation by others of beneficiaries who are unborn or whose identities are not reasonably ascertainable, and under more modern versions, beneficiaries who may be alive and known but who are minors or otherwise legally incapacitated.

Section 301 is the general and introductory section, laying out the scope of the article. The representation principles of this article have numerous applications under the Act. The representation principles apply for purposes of settlement of disputes, whether by a court or nonjudicially. They apply for the giving of required notices. They apply for the giving of consents to certain actions. Among the many practical, and in some cases, day-to-day administrative issues to which the representation principles of Article 3 can be applied, are:

(1) Modification or termination of a trust upon the consent of the beneficiaries, with or without the consent of the settlor (Section 410);

(2) Notice to qualified beneficiaries of a proposed trust combination or division (Section 415);

(3) Appointment of successor trustee upon agreement of qualified beneficiaries (Section 704(c)(1));

(3) Appointment of successor trustee upon agreement of qualified beneficiaries (Section 704(b)(1));

(4) Notice to qualified beneficiaries of resignation of trustee (Section 705);

(5) Notice of trustee's report (Section 813);

(6) Nonliability of trustee upon consent, release, or affirmance of beneficiary (Section 1010).

Section 301(b) deals with the effect of a consent, whether by actual or virtual representation. A consent by the representative bars a later objection by the person represented, but a consent is not binding if the person represented raises an objection prior to the date the consent on the person's behalf would otherwise become effective. The possibility that a beneficiary might object to a consent given on the beneficiary's behalf will not be germane in many cases because the person represented will be unborn or otherwise not reasonably ascertainable. But there are situations where the representation principles of this article can apply to adult and competent beneficiaries. For example, while the trustee of a trust entitled to a pourover devise has authority under Section 303 to represent the trust beneficiaries in the approval of the personal representative's account, such consent would not be binding on a trust beneficiary who objects to the representation.

Section 302 deals with the effect of a consent by the holder of a general testamentary power of appointment. (Revocable trusts and presently exercisable general powers of appointment are covered by Section 604, which grant the settlor or holder of the power all rights of the beneficiaries or persons whose interests are subject to the power). Absent a conflict of interest, the holder of a testamentary general power of appointment can bind those whose interests are subject to the power.

Section 303 provides that a fiduciary, absent conflict of interest, may represent and bind the beneficiary or beneficiaries of the respective fiduciary relationship, whether of an estate, trust, conservatorship, or guardianship. The section also allows a parent without a conflict of interest to represent and bind a minor or unborn child. A typical example of conflict of interest is a trustee who seeks approval of an accounting of an estate for which the trustee is acting as personal representative.

Section 304 is the virtual representation provision. It provides for representation of and the giving of a binding consent on behalf of a minor, incapacitated, or unborn person, or of a person whose identity or location is unknown and not reasonably ascertainable, by another beneficiary having a substantially identical interest with respect to the particular issue. Under this section, a person can be bound by a virtual representative only if (1) the person is not otherwise represented under one of the other sections of this article; and (2) there is no conflict of interest between the representative and the person represented.

Section 305 authorizes the court to appoint a representative to represent the interests of unrepresented persons or persons for whom the court concludes the other available representation might be inadequate. A representative may be

appointed to represent a person in an ongoing proceeding or to approve a settlement, whether judicial or nonjudicial. The reference to "representative" is placed in brackets to signal to the enacting state to substitute whatever term, such as guardian ad litem, that it normally uses. To encourage some flexibility in how the appointed representative approaches the job, the representative, in approving a settlement, may consider general family benefit.

Article 4
Creation, Validity, Modification, and Termination of Trusts

This article may be divided into three parts. Sections 401- 407 lay out the basic requirements for creating a trust. Sections 409- 415 specify the rules on the modification and termination of trusts. Section 408, a special provision limited to charitable trusts, covers both the creation of charitable trusts as well as their modification and termination.

Creation and Validity of Trusts (Sections 401-407)

Most of the requirements in the Act for the creation of a trust are straightforward and fairly conventional. This set of provisions develops a three-part classification system for trusts - private, charitable, and honorary. Private trusts require an ascertainable beneficiary, charitable trusts by their very nature are created for the public at large. The final category, honorary trusts, refers to noncharitable trusts but without ascertainable beneficiaries. This final category includes trusts for animals and trusts for other noncharitable purposes (e.g., trust to maintain cemetery lot).

The Uniform Trust Act pays particular attention to the increasing use of revocable trusts. The provisions relating to revocable trusts are concentrated in Article 6, but relevant provisions are also found elsewhere, including in this article. While the treatise writers and Restatement are unanimous that settlors of self-declared trusts may subject assets to the trust simply by listing them in the instrument, the issue of whether each asset needs to be specifically registered in the name of the trustee continues to be litigated. See. e.g., In re Estate of Heggstad, 20 Cal. Rptr. 43 (Ct. App. 1993). Section 401(b) resolves the debate by providing that a trust instrument may contain language subjecting identified property to a self-declared trust.

The sensitivity to revocable trusts is also reflected in the Act's provision on the doctrine of merger. Under this doctrine, as classically stated, no trust is created or an existing trust is "merged" if all legal and equitable interests are vested in the same person. A common situation where the traditional doctrine of merger technically applies but is often ignored in practice involves a revocable trust which names the settlor as sole trustee, with the remainder pouring back into the individual's probate estate. Under the traditional doctrine of merger, such a trust can never exist. Finding no particular social evil in such pourback arrangements, Section 402(a)(4) specifically excepts a pourback arrangement from the merger doctrine.

The Act does not specifically require that a trust be evidenced by a writing, but Section 405 does clarify that the execution of trusts is subject to the state's other law on when legal documents must be in writing (e.g., statute of frauds or statute on when real estate deeds must be in writing). This is contrary to a few trust statutes, such as the trust acts in California and Texas, which have detailed provisions on when a trust must be reduced to writing.

Section 406 addresses the creation of trusts for animals. To avoid the common law conclusion that such trusts were invalid because there was no legal person capable of enforcement, the settlor in the terms of the trust, otherwise the court, is authorized to appoint a person to enforce the trust. Because trusts for animals are sometimes overfunded, provision is made for distribution of any excess.

Modification and Termination of Trusts (Sections 409-415)

Sections 409 through 415 provide a series of overlapping rules on when a trust may be terminated or modified other than by its express terms. The overall objective of these sections is to liberalize the common law rules but without losing sight of the principle that preserving the settlor's intent is the paramount concern. Section 409 lists the circumstances when termination of the trust is automatic. This includes termination by revocation or pursuant to the trust's terms, or termination if the purposes of the trust have been fulfilled or become unlawful, impossible to achieve, or contrary to public policy.

Sections 410 through 415 lists situations where modification or termination requires some action, either by the court, the trustee, or the beneficiaries. Termination or modification may be allowed upon beneficiary consent (410) or by the court in response to unanticipated circumstances or if the purposes of the trust have been achieved or have become illegal or impossible to achieve (411). A trust may be modified to terminated by the court if continued administration

under the trust's existing terms would be uneconomical, or terminated by the trustee if the trust has a value of less than $50,000 (412). Trusts may be reformed to correct a mistake of law or fact (413), modified to achieve the settlor's tax objectives (414), or divided or consolidated (415).

Section 410 addresses termination or modification by beneficiary action, with or without the consent of the settlor. Subsections (a) and (b) restate long-established doctrine. Subsection (b) allows an irrevocable trust to be modified or terminated upon the unanimous consent of the settlor and beneficiaries (a revocable trust can of course be revoked by its settlor - see Section 602). Subsection (a) allows for termination or modification by unanimous agreement of the beneficiaries. However, termination by beneficiary action alone is permitted only if continuation of the trust is no longer necessary to achieve a material purpose. While inclusion of a spendthrift provision may be a material purpose sufficient to bar termination of a trust, this is not an automatic presumption.

Subsection (d) permits modification or termination upon agreement of less than all of the beneficiaries. This situation typically arises not because a beneficiary has objected to a proposed termination or modification, but because obtaining a consent is impracticable or impossible because the beneficiary is a minor, incapacitated, or unborn, or the beneficiary's identity is not readily ascertainable. Before approving such a termination or modification, the court must determine that (1) the proposed termination or modification otherwise meets the requirements of this section (settlor has approved proposal or continuation of trust on same terms not necessary to achieve material purpose); and (2) appropriate steps have been taken to protect the rights of the nonconsenting beneficiaries. Such protective steps might include the purchase of an annuity or allowing only a partial termination.

Circumstances frequently change following the date a trust becomes effective, often in ways not anticipated by the settlor. This has long been recognized through the doctrine of administrative deviation, which allows for modification of an administrative provision due to unanticipated circumstances. Concluding that the traditional doctrine of administrative deviation is too limiting, a number of states have enacted statutes liberalizing the doctrine, either by extending the doctrine to dispositive provisions or by making it easier to modify administrative terms. The Uniform Trust Act builds on this state experience. Section 411 allows the court to modify either the dispositive or administrative terms of a trust or terminate the trust if, because of unanticipated circumstances, modification or termination will substantially further the settlor's purposes in creating the trust. The court may modify or terminate a trust if the purposes of the trust have been achieved or have become illegal or impossible to achieve. The court may modify an administrative term if continuation of the trust on its existing terms would impair administration or be impracticable or wasteful.

Section 412 permits modification or termination of uneconomic noncharitable trusts. The rules with respect to uneconomic charitable trusts are addressed in Section 408 (discussed below). For very small trusts, this section grants the trustee a right to terminate the trust without condition unless this power is expressly limited by the terms of the trust. A $50,000 benchmark is suggested.. For larger trusts, court approval is required. In deciding whether a trust should be terminated or modified under this section, the court must determine whether continuation of the particular trust is justified considering the costs of administration involved. The court may also appoint a new trustee.

Inter vivos trusts have traditionally been correctable for mistake, but this repair device has not been available for trusts created by will. Section 413, which codifies Section 12.1 of the tentative draft of the Restatement Third (Property): Donative Transfers, permits reformation of all types of trusts on grounds of mistake. Special rules apply with respect to furthering the settlor's tax objectives. Section 414, tracking Section 12.2 of the same Restatement, requires that the terms of the trust be construed to achieve the settlor's tax objectives, including the ability to modify the trust in a manner that does not violate the settlor's probable intention. The section also clarifies that such a change may be made retroactive.

Section 415 permits combination or division of trusts, without court approval if the combination or division does not impair the rights of any beneficiary or adversely affect achievement of the trust purposes. Such a division is frequently done to allow for better utilization of generation-skipping tax exemptions. Combination of trusts is most frequently used to reduce costs and administrative burdens when identical trusts are created by different members of the same family.

Charitable Trusts (Section 408)

This section does not comprehensively address the topic of charitable trusts but focuses only on specific issues unique to this type of trust. Charitable trusts, because they are included within the definition of "trust" (see Section 102(18)), are subject to the other provisions of the Act.

Subsection (a) is not an innovative provision. It simply restates the standard list of charitable purposes from the Statute of Queen Elizabeth of 1601. This list, and its huge case law progeny, has served us well over the centuries and the

drafting committee sees no reason to upset such a well-settled tradition. This subsection also ratifies the established estate planning technique allowing the trustee to select the charitable beneficiary or purposes for which distributions may be made.

The innovative provisions are subsections (b) and (c), which liberalize the rules on cy pres. The doctrine of cy pres has in recent years been a fertile source of much academic commentary. The topic is important not only for trusts but also for other forms of charitable giving. Under traditional doctrine, if a specific charitable purpose fails, the court seeks to determine whether the settlor had a general charitable intent. If so, the trust property is diverted to other charitable uses. If not, the trust fails. This section, on the other hand, assumes that in the great majority of cases the settlor would prefer that the gift not fail but be used for other charitable purposes. Consequently, unless the terms of the trust provide to the contrary, a charitable trust does not fail if a specific charitable purpose becomes impracticable, unlawful, impossible to achieve, or wasteful. Rather, the court, applying cy pres, must apply or distribute the trust property, in whole or in part, in a manner consistent with the settlor's charitable purposes. Furthermore, while a settlor is free to provide a gift over in the event the original charitable purpose of the trust fails, such a provision, if made in favor of a noncharitable beneficiary, is valid for only 30 years from the date of the trust's creation.

Subsections (d)-(f) address procedural issues. While the Act does not require that the Attorney General receive all notices provided to qualified beneficiaries, subsection (d) requires that the Attorney General be notified in advance of a proposed termination of a charitable trust with a value of less than $50,000. The Act does not otherwise impact the state's existing law on the role of the Attorney General, including requirements that the trustee file annual reports with the state and be given notice of any judicial proceeding involving a charitable trust. Subsection (e) adopts the practice followed by the many donor-advised endowment funds that have sprung up in recent years. While a settlor of an irrevocable trust is normally without standing to enforce the trust, this subsection, following Wisconsin's lead, provides that the settlor is an interested person in a proceeding brought to modify or enforce a charitable trust. Subsection (f) recognizes the special interest that named recipients have in enforcing a trust. Under the Act, charitable organizations expressly named to receive benefits are granted the rights of qualified beneficiaries.

Article 5
Creditor's Claims; Spendthrift Provisions; Discretionary Trusts

This article addresses more than just the provisions prohibiting beneficiaries from assigning their interests or their creditors from collecting from the trust. It also addresses rights of creditors based on the nature of the beneficiary's interest. In other words, many trusts have two lines of defense against creditor claims. The creditor will first encounter the spendthrift bar. But assuming this bar can be bypassed, the creditor may still not be able to collect, particularly if distributions to the beneficiaries are in the discretion of the trustee.

Sections 501 and 502 are general provisions. Section 501 specifies the rights of creditors and assignees whose claims are not precluded by a spendthrift bar; Section 502 describes the effect of a spendthrift provision. The remaining sections address special situations. Section 503 lists the categories of creditors whose claims are excepted from a spendthrift provision. Section 504 states the creditor rules for discretionary trusts and trusts providing for distributions according to some sort of standard. Section 505 addresses creditor claims against a settlor, whether the trust is revocable or irrevocable, and if revocable, whether the claim is made during the settlor's lifetime or incident to the settlor's death. Section 506 provides a creditor with a remedy if the trustee fails to make a required distribution within a reasonable time. Section 507 clarifies that a trust is not subject to the trustee's personal debts, particularly in the event of the trustee's bankruptcy or insolvency.

Section 501. Rights of Beneficiary's Creditor of Assignee Without Spendthrift Provision.

To the extent a beneficiary's interest is not protected by a spendthrift provision, the creditor can attach the beneficiary's interest. But whether the creditor will be able to collect or not may depend on the nature of the beneficiary's interest, whether it is discretionary with the trustee or subject to a standard of distribution (see Section 504). Second, following the lead of Restatement (Third) of Trusts, the court with jurisdiction over the trust need not award the creditor the full amount of the claim. The court is to grant such relief as is appropriate, following consideration of the beneficiary's actual needs and the needs of dependent family.

This section does not attempt to prescribe the procedures for collecting from a beneficiary's interest, preferring instead to leave that issue to the enacting state's law on creditor rights. The section does clarify, however, that any order

obtained against the trustee, whatever state procedure may have been utilized, may extend to future distributions to be made to the beneficiary.

Section 502. Spendthrift Provision: General

This section ratifies the use of spendthrift provisions. The effect of a valid spendthrift provision is to prevent a creditor from attaching a distribution from the trust prior to its receipt by the beneficiary. For spendthrift protection to apply, the instrument must include a statement to that effect. Unlike the law in at least a few states, this section does not provide that a trust is automatically spendthrift. Also, to obtain spendthrift protection, the settlor must address both "voluntary" and "involuntary" transfers, i.e., the Act does not permit a settlor to provide that a beneficiary may assign but that the creditors may not collect, or vice versa. This section does not distinguish between rights in income and rights in principal. Spendthrift provisions are valid as to both accounting categories.

The section also includes a rule of construction, patterned after Texas law. The use of the words "spendthrift trust" or words of similar import is sufficient to restrain both the voluntary and involuntary transfer of a beneficiary's interest.

Beneficiaries will on occasion assign their interest notwithstanding a valid spendthrift provision. While such assignments are unenforceable and revocable by the beneficiary at any time, the Act follows standard doctrine by providing that until revoked, a trustee *may* honor such an assignment.

Section 503. Exceptions to Spendthrift Provision

This section recognizes that certain categories of creditors are not subject to the spendthrift bar. Consistent with federal bankruptcy law, the statutes and case law of many states, and the Restatement of Trusts, an exception is recognized for the support claims of the beneficiary's children and current or former spouse. Notwithstanding a spendthrift provision, the child or current or former spouse may obtain, in an appropriate judicial proceeding, an order to attach present or future distributions to be made to or for the benefit of a beneficiary. However, whether an order will result in actual collection by the beneficiary may depend on the nature of the beneficiary's interest (see Section 504).

An exception is also created for governmental claims. Federal preemption guarantees that certain claims, such as claims by the Internal Revenue Service, may bypass a spendthrift provision no matter what the Act might say. For state claims, this section recognizes that states take a diversity of approaches on how they treat state claims, some granting a priority to all state claims, regardless of their nature, and others applying different rules depending on whether the claim is for unpaid state taxes, for care provided at an institution, or for more general charges. Acknowledging this diversity, this section leaves to the other statutes of the enacting jurisdiction the question of whether a particular state claim will be subject to the spendthrift bar.

Finally, an exception is created for a judgment creditor who has provided services for the protection of a beneficiary's interest.

The Act is less expansive than Restatement (Second) Trusts Section 157 in its creation of exceptions for preferred creditors. Unlike the Restatement, no exception is created for providers of necessary services, the drafters recognizing that because most such cases involve claims of the state, the subject is best addressed by separate state-specific legislation.

Section 504. Discretionary Trust and Trust Subject to Standard

The fact that a creditor may fit within one of the exceptions to spendthrift protection recognized by Section 503 does not mean that the creditor can collect from the trust. The creditor must also bypass the hurdles possibly created by the nature of the beneficiary's interest. If a creditor fits within an exception to spendthrift protection, the creditor, due to the ability to attach the beneficiary's interest, may intercept payments the trustee is required to make by the express terms of the trust (e.g., mandatory income). As to payments within the trustee's discretion or payments to be made subject to a standard, the creditor may reach only those payments the trustee decides to make, whether or not the trust contains a spendthrift provision.

With only one exception, under the Act a creditor does not succeed to a beneficiary's right to sue the trustee for an abuse of discretion or failure to comply with a standard. The exception relates to a child or current or former spouse who has a judgment against a beneficiary for support. The court is to award the spouse or child such amount as is equitable under the circumstances but not in excess of the amount the trustee would have been required to distribute to the

beneficiary had the trustee not abused the discretion or failed to comply with the standard.

Section 505. Creditor's Claim Against Settlor

This section addresses creditor claims against a settlor, whether the trust is revocable or irrevocable. For revocable trusts, the section covers creditor claims both while the settlor is alive and at the settlor's death. Unlike various Pacific islands, and more recently, Alaska, Delaware, Nevada, and Rhode Island, the Act does not allow a settlor to retain a beneficial interest in the trust and at the same time use the trust to shield assets from creditors. Following traditional doctrine, a settlor's creditors may reach whatever amounts the trustee could have paid to or for the settlor's benefit.

For revocable trusts, this section states the obvious - during a settlor's lifetime a revocable trust is fully subject to the claims of the settlor's creditors. More difficult is the question of liability for claims following the settlor's death, an issue widely discussed in the estate planning community in recent years. This section establishes that a revocable trust is not immune from the claims of creditors but that to the extent the probate estate is insufficient, the trust assets are liable for the settlor's debts, expenses of administration, funeral expenses, and allowances to the family. This section is not designed to address all creditor issues that may arise in connection with revocable trusts, such as possible liability for claims of other nonprobate assets. These issues, which extend well beyond the law of trusts, are addressed in new Section 6-102 of the UPC, approved by the Uniform Law Commissioners in 1998.

This section also applies to powers of withdrawal. Under the Act, holders of powers of withdrawal are treated the same as holders of a power of revocation because of their equivalent power over the trust. Consequently, during the period the power of withdrawal may be exercised, the property subject to the power is subject to the claims of the power holder's creditors. But an exception is created for the holders of Crummey or 5 and 5 powers. Recognizing the special and limited nature of such powers, upon the lapse or release of a Crummey or 5 and 5 power, property which was subject to the power is exempt from claims of the holder's creditors .

Section 506. Overdue Distribution

This section on overdue payments by a trustee applies whether or not the trust contains a spendthrift provision. The theory is that a trustee should not be allowed to defeat a beneficiary's creditors by delaying required distributions. Following a reasonable administrative period in which to make the distribution, the section treats the trustee as the beneficiary's agent and subjects the distributable assets to creditor claims just like any other of the beneficiary's personal assets.

Section 507. Personal Creditors of Trustee

This section clarifies that the fact a trustee holds legal title to the trust assets does not mean that the trustee is to be treated the same as an individual owner. Under this section, the trust property is protected against claims of the trustee's personal creditors even if the trustee becomes insolvent or bankrupt.

Article 6

Revocable Trusts

Given the widespread use of the revocable trust as an alternative to probate, this article takes on increased importance. Each section of this short article deals with issues of significance not totally settled under current law.

Section 601. Capacity of Settlor of Revocable Trust

This section specifies the capacity standard for a revocable trust. The section assumes that the vast majority of revocable trusts are created as alternatives to wills. Consequently, the capacity standard for wills as opposed to irrevocable trusts is appropriate. The capacity standard for wills applies not only to the creation of a revocable trust but also to its amendment, revocation, and the addition of property.

Section 602. Revocation or Amendment of Revocable Trust

Subsection (a) places the Uniform Act in line with the five states (California, Iowa, Montana, Oklahoma, and Texas) which reverse the common law presumption that a trust is irrevocable unless its terms provide otherwise. Under the Act, if the terms of the trust do not say otherwise, the trust is revocable. The drafting committee concluded that between the two options, a presumption of revocability is the better choice. Because most trust instruments state expressly whether

the trust is revocable or irrevocable, which way the presumption tilts is important in only a small minority of cases. The presumption of revocability is subject to two exceptions. First, it does not apply to trusts created under instruments executed prior to the date of enactment. Second, it does not apply to trusts created in states which presume that a trust is irrevocable unless stated otherwise.

Subsection (b) addresses the problem of revocation of joint trusts. Trusts created jointly by a married couple have become quite common in recent years, not only in community property states where they originated as a device for placing community property in trust. Reflecting this community property background, the rules on revocation differ depending on whether the trust includes community property. Because community property does not change its character upon its withdrawal from the trust, to the extent the trust consists of community property, either spouse may revoke the trust, but an amendment must be approved by both spouses. With respect to other property, each settlor may revoke or amend the trust to the extent of the trust property attributable to that settlor's contribution.

Subsection (c) specifies the standard methods of revocation. Like nearly everything else in the Act (see Section 103), this provision may be superseded by the terms of the trust. However, absent language in the terms of the trust making the specified method exclusive, the trust may be revoked by substantially complying with the method specified in the trust's terms or by any method manifesting clear and convincing evidence of the settlor's intent, including by a provision in the will.

Subsections (e) and (f) address the extent to which the settlor's agent or conservator may revoke a revocable trust. An agent may revoke the principal's revocable trust only if the terms of the trust or power of attorney expressly grant the agent that power. A conservator may revoke the settlor's trust if authorized by the court supervising the conservator. The terms of the trust may prohibit such a revocation, however.

Section 603. Direction of Settlor.

This section codifies a useful provision of California law. Reflecting the philosophy that the settlor of a revocable trust is in complete control, the section protects a trustee in following the settlor's direction, even if the direction is inconsistent with the terms of the trust.

Section 604. Settlor's Exercise of Rights of Settlor; Presently Exercisable Powers of Withdrawal

Subsection (a) confirms the basic approach to revocable trusts while the settlor is alive - the settlor is in complete control. While the trust is revocable and the settlor has capacity, the duties of the trustee are owed exclusively toe the settlor and the rights of the beneficiaries are subject to the settlor's complete control. The implications of this section can be seen throughout the Act. For example, Section 813 requires a trustee to provide a copy of the trust instrument upon request of a beneficiary. But as long as the settlor is alive and has capacity, the trustee's duty in this regard flows only to the settlor.

Subsection (b) covers what happens when the settlor becomes incapacitated. If represented by a conservator, guardian, or agent under a durable power of attorney, the settlor remains in exclusive control and the conservator, guardian, or agent may act for the settlor to the extent authorized by local law or the power of attorney (see Section 602). However, if the trustee and other fiduciary are the same person or if the settlor is not represented, the rights of the beneficiaries will be held by the beneficiaries.

Subsection (c) establishes that the holder of a power of withdrawal is treated the same as the holder of a power of revocation because the two are functionally equivalent. An example of such a trust is a trust created for a spouse which grants the spouse an unlimited lifetime power of withdrawal.

Section 605. Limitation on Action Contesting Validity of Revocable Trust

Will contests must normally be brought within a relatively short period following admission of the will to probate. Few states have enacted specific time limits for contest of revocable trusts. To provide the beneficiaries with some certainty, subsection (a) establishes a two year from death cutoff for contesting the trust. However, the trustee may shorten the period to 120 days by giving a notice as long as the notice informs the recipient of the time limit and of whether the person is a beneficiary .

This section does not require a trustee to withhold distribution until the end of the contest period. To encourage expeditious distribution of the trust property, subsection (b) permits a trustee, immediately following the settlor's death,

to assume without liability that the trust is valid absent knowledge of a pending judicial proceeding or notification by a

potential contestant of a possible action, followed by its filing within 30 days. But as provided in subsection (c), until a contest is barred a beneficiary of what turns out to have been an invalid trust is liable to return any distribution received.

Article 7
Office of Trustee

This article contains a series of rules dealing with the office of trustee, all of which may be modified by the terms of the trust. Section 701 specifies the procedure for accepting or declining a trusteeship. Acceptance by the trustee will normally occur upon delivery of a signed acceptance or by knowingly exercising the powers of the trustee. Section 702 addresses trustee bond, although because bond is required only if ordered by the court, bond will rarely be required under the Act. Section 703 deals with the office of cotrustee. Contrary to the law in some states, this section permits cotrustees to act by majority decision. Each cotrustee must also participate in the administration of the trust and must take reasonable steps to prevent another trustee from committing a breach of trust and to compel a cotrustee to redress a breach of trust. In the event of a vacancy in the trusteeship, the vacancy need not be filled unless the terms of the trust so require. The remaining trustee or trustees may act for the trust.

The extent to which a trustee can delegate to a cotrustee is a particularly important topic. Section 703 prohibits a trustee from delegating to another trustee or trustees functions the settlor expected the cotrustee to perform personally. No inquiry on this topic is made, however, and the right to delegate is unlimited, if the function is the type of ministerial act normally delegated by trustees or if the inability to delegate would cause adverse tax consequences to the trustee or the trust.

Sections 704 through 707 address changes in the office of trustee. Section 704 lists the events which trigger a vacancy in the trusteeship and prescribes the procedure for filling the vacancy. The terms of the trust are controlling, but if the terms are silent or ineffective, the vacancy may be filled either by a person designated by unanimous agreement of the qualified beneficiaries, or by a person appointed by the court. The court may also appoint an additional trustee when necessary for the trust's administration.

Sections 705 and 706 address two of the key events by which a trustee may be changed - resignation and removal. Traditionally, absent a specific provision in the trust instrument a trustee could resign only with court approval. To avoid such a cumbersome process, many trust instruments provide that a trustee may resign by providing notice to specified beneficiaries. Section 705 adopts this approach. The trustee may resign upon 30 days written notice, to the settlor if the trust is revocable, to the qualified beneficiaries for irrevocable trusts. Notice of the resignation must also be given to any cotrustees. Section 706 addresses trustee removal. The section allows for removal under four specified grounds; breach of trust; lack of cooperation among cotrustees; persistent and substandard investment performance; and if removal would be in the best interest of the beneficiaries because of changed circumstances or the trustee's unfitness or unwillingness to perform the duties of office. This final category might be appropriate to apply in cases where a bank merger substantially changes the character of the trust institution.

Section 707 confirms the trustee's duty to deliver trust property to a successor trustee. Until this task is accomplished, the trustee who has resigned or been removed continues to have the duties of the trustee and the powers to protect trust property. The resigning or removed trustee's responsibility continues, however, only in the absence of a cotrustee. The section also does not apply if the court gives specific directions, a frequent occurrence when a trustee is removed.

Section 707 in addition addresses the responsibility for winding up the work of a trustee who has died or been adjudicated incompetent. Unless a cotrustee remains in office, responsibility for protection of the trust property is placed on the former trustee's personal representative or guardian or conservator, with these interim responsibilities to terminate once a successor trustee is in office and the trust property delivered.

Sections 708 and 709 deal with trustee compensation and reimbursement. If the terms of the trust do not specify the trustee's compensation, the trustee is entitled to compensation that is reasonable under the circumstances. The trustee is also entitled to reimbursement for expenditures properly incurred in administration, and for expenses not properly incurred but which turned out to benefit the trust. Compensation may be paid without court order (see Section 816(16)).

Article 8
Fiduciary Administration

This article states the fundamental duties of a trustee and lists the trustee's powers. The duties listed are not new. All are ultimately derived from the trustee's duty of loyalty to the beneficiaries and responsibility to exercise prudence and reasonable care, duties basic to the law of trusts. But how the particular duties are formulated and applied has changed over the years. This article was drafted where possible to conform with the 1994 Uniform Prudent Investor Act. The Uniform Prudent Investor Act, while it focuses on investment decisions, also prescribes duties of wider applicability. These duties of broader scope include the duties relating to loyalty (Section 802), impartiality (Section 803), administrative costs (Section 805), and delegation (Section 807). Where the two acts overlap, states are to enact the provisions of this article and not those of the Prudent Investor Act.

As permitted by Section 103, a settlor is generally free to modify the duties prescribed by this article. However, the settlor is not free to override the trustee's fundamental obligation to act as a fiduciary, in good faith, and with regard to the purposes of the trust and the interests of the beneficiaries. Certain of the trustee's reporting obligations are also nonwaivable (see Section 813).

Section 801. Duty to Administer Trust

This section recites the trustee's traditional responsibility to administer the trust in good faith and in accordance with its terms and purposes and the interests of the beneficiaries.

Section 802. Duty of Loyalty

This section does not attempt to state all aspects of the duty of loyalty. Instead, subsections (a) and (b) recite the general rules; subsections (c)-(g) focus on some but not all possible problem areas. Given the myriad of difficult fact

general rules; subsections (c)-(g) focus on some but not all possible problem areas. Given the myriad of difficult fact situations which arise in this area, it is best to leave the resolution of many of these questions to the courts and to the rich case law background.

The duty of loyalty imposes an obligation on a trustee to administer the trust solely in the interests of the beneficiaries (subsection (a)). Among other things, this grants the beneficiaries a right to undo a transaction affected by a conflict of interest. This right to undo the transaction is barred, however, by a variety of events, such as approval by the court or prior beneficiary approval (subsection (b)).

A beneficiary wishing to undo a transaction ordinarily has the burden of proof on establishing that the transaction was affected by a conflict between the trustee's personal and fiduciary interests.

For transactions involving a trustee's personal purchase, lease, etc., of trust property, the conflict is apparent. The conflict is often not as obvious where the trustee's role is less direct. Subsection (c) provides a rule for these less obvious cases by making presumptively voidable transactions between the trust and specified persons with significant connections to the trustee. Included on the list are the trustee's spouse and other close relatives, the trustee's agent or attorney, and a corporation or other enterprise, or its affiliate, in which the trustee has an interest that might affect the trustee's best judgment.

Subsection (d) addresses a significant problem area - transactions between a trustee and a beneficiary outside of the trust where the trustee has a possibly dominant position. This subsection creates a presumption that such a transaction is an abuse by the trustee of a confidential relationship and is consequently voidable at the beneficiary's election. But to obtain the presumption, the beneficiary must show that the transaction enabled the trustee to obtain an advantage over the beneficiary. Also, the presumption is rebutted by the trustee upon a showing that the transaction was fair to the beneficiary.

Subsection (e) addresses what is known as the "opportunity" doctrine, a doctrine frequently applied to corporate directors and officers. Under this doctrine, a transaction engaged in by the trustee is deemed to involve a conflict between personal and fiduciary interests if the transaction concerned an opportunity properly belonging to the trust.

Bowing to political realities and the substantial majority of states which have in recent years enacted statutes on the subject, subsection (f) allows a trustee to invest in a "proprietary" mutual fund from which it, or an affiliate, receives a fee for providing administrative or other services. The exception is limited, however. While an investment in a proprietary fund is not per se a prohibited act of self-dealing, the trustee remains subject to other aspects of the duty of loyalty and the duty to invest with prudence. Also, the trustee must disclose to the qualified beneficiaries the rate and method by which it is being compensated for providing services to the fund.

Subsection (g) recognizes that a trustee should be permitted to negotiate in freedom regarding the terms and conditions

of the trustee's appointment and compensation. Just as importantly, the subsection recognizes that individuals frequently act in multiple and overlapping fiduciary roles. A trustee is permitted to engage in a transaction with another trust, decedent's estate, or conservatorship of which the trustee is a fiduciary or a beneficiary has an interest. The trustee is not relieved of fiduciary responsibility for the transaction, however. The resulting transaction, whether relating to the trustee's appointment, compensation, or transaction with another fiduciary account, must be fair to the trust beneficiaries.

Subsection (h) ratifies a technique that can avoid many duty of loyalty issues. Upon petition by a trustee or beneficiary, the court may appoint a special fiduciary to make a decision with respect to a transaction that might involve a conflict of interest.

Section 803. Impartiality

This section, which restates the impartiality prong of the duty of loyalty, is copied from the Uniform Prudent Investor Act.

Section 804. Prudent Administration

This section states the basic standard of care, which is one of prudence. This standard is derived from the Uniform Prudent Investor Act, and is also the cornerstone of the Restatement (Third) of Trusts: Prudent Investor Rule, upon which the Uniform Prudent Investor Act was based.

Section 805. Costs of Administration

This admonition to incur only reasonable costs is taken directly from the Uniform

Prudent Investor Act.

Section 806. Trustee's Skills

The duty of a trustee to apply the full extent of the trustee's skills is not new but is found in both the Uniform Probate Code and the Restatement (Second) of Trusts. This section applies a double test. A trustee with higher skills is always held to a standard based on those skills. But also held to a higher standard are trustees with lesser skills who hold themselves out as possessing higher skills.

Section 807. Delegation by Trustee

This is yet another one of the sections derived from the Uniform Prudent Investor Act and the Restatement (Third) of Trusts: Prudent Investor Rule. While traditionally treated as a duty, the section is really more of a powers provision, clarifying that a trustee has the power to delegate. Traditionally, the duty or power to delegate was phrased in the negative. A trustee could not delegate except for limited exceptions. This section, and the sources upon which it is based, state the trustee's power to delegate in the affirmative. The emphasis is on protecting the trustee from liability for

making delegations and in establishing appropriate standards for a delegation.

Section 808. Powers to Direct

Trust instruments frequently grant nontrustees the authority to perform certain actions traditionally handled by a trustee. For example, a beneficiary may be given authority to direct investments, a practice prevalent among trusts holding employee retirement funds. Or a nontrustee may be given authority to direct the trustee with respect to the retention and management of the settlor's closely-held business. To encourage trustees to comply with powers to direct, this section protects a trustee who honors the exercise of such a power. But the section goes further by requiring that the trustee actually comply with the exercise of the power. Noncompliance is excused only if the attempted exercise is manifestly contrary to the terms of the trust or the trustee has reason to believe that the exercise violates a fiduciary duty the holder of the power owes to the beneficiaries of the trust.

The section also clarifies the role of the power holder, who often acts similar to a trustee in function if not in title. The holder of a power to direct is presumptively a fiduciary who, as such, is required to act in good faith, with regard to the purposes of the trust, and with regard to the interests of the beneficiaries.

Section 809. Control and Protection of Trust Property

This section codifies the trustee's traditional duty to take control of and protect the trust property.

Section 810. Separation and Identification of Trust Property

This section addresses in one place the duties to earmark the trust property and to keep the trust property separate from the trustee's own assets. Under subsection (a), the prohibition against commingling the trust property with the trustee's own property, which is a very serious breach of trust, is absolute.

Subsection (b) addresses earmarking, that is, the requirement that trust property be properly designated as property of the particular trust. The issue with which the drafting committee has struggled is what is meant by the term "earmarking." Saying that the interest of the trust must clearly appear merely begs the question. Clearly appear in what form and on whose records? The solution the drafting committee has developed is to require that the trustee designate the assets in such a way that the interest of the trust clearly appears in the records of a third party. Regulated financial service institutions, because they are subject to audit by federal or state authorities, are exempted from this requirement. They are permitted to designate the trust assets such that the interests of the separate trusts would appear only in their own records.

The section also creates an exception for joint investments. When a trustee acts as trustee for more than one trust, efficiencies are often achieved by making joint investments of the trust funds. However, because the interest of the particular trust would appear only in the trustee's own records such joint investments would technically constitute a violation of the duty to earmark as stated in subsection (b). While a trustee is not allowed to commingle trust funds with those of the trustee or, more generally, with those of another person, subsection (c) does allow the trustee to jointly invest trust funds with those of another trust of which the trustee is also trustee.

Section 811. Enforcement and Defense of Claims

This section, like Section 809, restates traditional duties of a trustee without substantive change.

Section 812. Former Fiduciaries

Possible liability of a trustee for the actions of a predecessor can be an issue whenever a trustee takes over from another fiduciary. Sometimes the concern involves the actions of a prior trustee. Sometimes the concern involves the actions of a personal representative from whom the trustee is receiving estate assets. The trustee is not directly liable for a breach of trust committed by the predecessor. Rather, the Act provides, in accordance with traditional doctrine, that trustees taking over from another trustee or other type of fiduciary may commit their own breach of trust by failing to take reasonable steps to compel the delivery of trust property, or by failing to take reasonable steps to redress a breach of trust known to the trustee to have been committed by the predecessor.

Section 813. Duty to Inform and Report

This is one of the more important sections of the Act. The duty to keep the beneficiaries reasonably informed is one of the trustee's fundamental responsibilities. Potential problems are often avoided simply by keeping the beneficiaries up to date. Keeping the beneficiaries reasonably informed also enables the beneficiary to enforce the beneficiary's rights under the trust and to prevent or redress a breach of trust.

Subsection (a) of this section states the general duty, which is derived from the common law but also updated. The trustee's duty to keep the beneficiaries reasonably informed extends only to the qualified beneficiaries, and not to those holding remote and often unascertainable interests. The obligation to promptly respond to a reasonable request for information is owed to all beneficiaries, however.

Subsections (b)-(f) state specific applications of the general duty. The most important of these applications is perhaps subsection (g). Subsection (g), consistent with Section 603, clarifies that while a trust is revocable and the settlor has capacity, the duty to provide information runs only to the settlor, who holds all of the rights otherwise granted to the beneficiaries.

But assuming that the trust is irrevocable or that the settlor has lost capacity, subsection (b)(l) requires the trustee to supply a beneficiary upon request with a copy of the trust instrument. The drafting committee intentionally rejected the approach that the trustee need supply the beneficiary only with those portions of the instrument that the trustee deems relevant, concluding that such a rule would be too restrictive.

Subsection (b)(2) addresses acceptance of the trusteeship, an action which the trustee must communicate to the qualified beneficiaries within 30 days. Special rules are also provided for revocable trusts, which this section and the Act

qualified beneficiaries within 30 days. Special rules are also provided for revocable trusts, which this section and the Act in general recognize are primarily will substitutes. Similar to the obligation imposed on a personal representative following the admission of a will to probate, subsection (b)(3) requires the trustee of a revocable trust to inform the qualified beneficiaries, within 30 days after the settlor's death, of the trust's existence. These two duties can overlap. If the death of the settlor happens to also be the occasion for the appointment of a successor trustee, the new trustee of the now formerly revocable trust would need to inform the beneficiaries both of the trustee's acceptance which, by necessity, would also inform the beneficiaries of the trust's existence.

Subsection (b)(4) deals with the sensitive issue of changes, usually increases, in trustee compensation. While a trustee may pay itself without seeking court approval (see Section 816(16)), the trustee must inform the beneficiaries in advance of the change.

Subsection (c) is influenced by Allard v. Pacific National Bank, 663 P. 2d 104 (Wash. 1983), in which the court surcharged a trustee for failing to give the beneficiaries advance notice of the sale of a parcel of real estate, which was the trust's sole asset. Cases subsequent to *Allard* have expanded this duty to include informing beneficiaries of proposed sales of interests in closely-held businesses. This subsection also extends the duty to sales or other dispositions of tangible personal property. However, disclosure is required only if the sale or other disposition involves assets that comprise in value a significant portion of the trust. But otherwise required disclosure is waived if it would violate other law, such as federal securities laws, or if disclosure would be seriously detrimental to the interests of the trust beneficiaries. This final exception might apply, for example, if disclosure would cause loss of the only serious buyer.

Subsection (d) addresses the trustee's duty to account, which is changed to a requirement to "report" to negate any inference that the report must be prepared in any particular format. The key is not the format chosen but whether the report provides the beneficiaries with the information necessary to protect their interests. Reports must be provided to the qualified beneficiaries annually and upon termination of the trust. Unless a cotrustee remains in office, a report must also be provided to the qualified beneficiaries upon a vacancy in a trusteeship. A report on behalf of a deceased or incapacitated trustee must be prepared by the trustee's personal representative or conservator or guardian. This coordinates with Section 707, which may place an obligation on the personal representative or guardian or conservator to manage the trust until the trust property is delivered to the successor trustee.

Subsection (e) allows a beneficiary, by a written consent, to waive the right to a trustee's report or other information required to be provided under the section. A beneficiary may also revoke a written consent previously given.

Section 813 is one of the few sections of in the Act not freely alterable by the terms of the trust. There are three exceptions. First, subsection (f) ratifies the so called "blind" trust. While the terms of a trust may not prohibit the trustee from providing beneficiaries with the information required under this section, such a prohibition is valid with respect to a beneficiary who is also the settlor. Second, subsection (f) allows a settlor to waive the right to a trustee's report and other required reporting with respect to beneficiaries under 25 years of age. Finally, subsection (c) permits the settlor to waive advance notice of a nonroutine transaction for which disclosure would otherwise be required.

Section 814. Duties With Regard to Discretionary Power

No matter how broad the discretion, a grant of discretion is never absolute. As this section makes clear, a trustee must always act in good faith and with regard to the purposes of the trust and the interest of the beneficiaries.

Sections 815-816. General and Specific Powers of Trustees

Section 815 states general principles; Section 816 is a listing of specific powers. As provided in Section 103, the Act is primarily a default statute, subject to override in the terms of the trust. Nowhere is this more true than with respect to the specific powers listed in Section 816. The trustee powers list in Section 816 is ultimately derived from the Uniform Trustees Powers Act but with many modifications. While the list in Section 816 is comprehensive, demands by third parties to see specific authorization in the instrument suggests that a detailed list of powers usually be included in the terms of the trust.

Certain powers are granted to trustees elsewhere in the Act, including the power to delegate (Section 807), to invest trust property (Article 9), to make joint investments with other trusts (Section 810), and to consolidate and divide trusts (Section 415).

Section 817. Proposal for Distribution.

This section is designed to facilitate distribution upon termination of a trust. Derived from a comparable provision of the Uniform Probate Code, upon being sent a proposal for distribution which mentions the time limit, a beneficiary has 30 days in which to object to the kind or value of asset received.

Article 9
Uniform Prudent Investor Act

This article provides a place for a jurisdiction enacting this Act to codify its version of the Uniform Prudent Investor Act. Also provided are instructions on how to modify the Uniform Prudent Investor Act to avoid overlap between the two acts.

Article 10
Liability of Trustees and Rights of Persons Dealing With Trustee

This article lists the actions which may be brought against a trustee, the methods by which damages are to be measured, and the methods for relieving a trustee from liability.

The remedies for a breach of trust, other than money damages, are listed in Section 1002. The remedies provided are both broad and flexible. They include orders to compel trustees to perform or not perform certain acts, to recover property of the trust, to remove the trustee, and to reduce or deny the trustee compensation. The measure of money damages provided in Section 1003 reflects two competing principles: (1) the trust should be restored to the position it

would have been in had the harm not occurred; and (2) the trustee should not be permitted to profit from the trustee's wrong. The Act resolves the tension between the two principles by charging the trustee with whichever figure is the higher. Consequently, damages are in all events to be set to at least restore the trust, but if the profit earned by the trustee is higher, the trustee must pay the higher amount.

Occasionally, a trustee profits because of the position of trust without having committed a breach of trust. Section 1004 holds a trustee accountable for such a profit.

Section 1005 expands and clarifies the ability to award costs and attorney's fees. In a judicial proceeding involving a trust, the court, as justice and equity may require, may award costs and expenses, including reasonable attorney's fees, to any party, to be paid by another party or from the trust that is the subject of the controversy.

Sections 1006 through 1010 address methods for relieving the trustee from liability. One method is to include an exculpatory provision in the terms of the trust. Under Section 1009, an exculpatory clause is effective except for intentional breaches, or for acts taken in bad faith or with reckless indifference to the purposes of the trust or the interest of the beneficiaries. But not all exculpatory clauses are enforceable even to that extent. Never enforceable is an exculpatory clause inserted into the instrument as a result of an abuse of a fiduciary or confidential relationship to the settlor. Rejecting the result in the celebrated case of Marsman v. Nasca, 573 N.E. 2d 1025 (Mass. Ct. App. 1991), the Act provides that an exculpatory clause drafted by or on behalf of the trustee is presumed to have been inserted as a result of an abuse unless the trustee proves that the clause was fair and that its existence and contents were adequately communicated to the settlor.

Sections 1007 and 1008 protect trustees exercising reasonable care in circumstances where liability has sometimes been imposed. Per Section 1007, a trustee acting in reasonable reliance on the terms of a written trust instrument is protected to the extent a breach of trust is attributable to such reliance. This might occur, for example, if extrinsic evidence establishes that a mistake of fact or law was made in the trust's creation, justifying retroactive reformation of the trust. Section 1008 protects a trustee who was unaware of an event, including marriage, divorce, performance of educati0on requirements, or death, which affects the trust's administration or distribution. However, the trustee is protected only if the trustee exercised reasonable care to ascertain that the event occurred.

Section 1010 provides for relief of trustee liability by beneficiary consent. A beneficiary is estopped if the beneficiary consented in advance, ratified a transaction which has already occurred, or otherwise released the trustee from liability. However, the trustee is not relieved from liability if the consent, release or ratification was induced by the trustee's improper conduct or if the beneficiary did not know of the beneficiary's rights or of the material facts the trustee knew or should have known with the exercise of reasonable inquiry.

Finally, a trustee may be relieved from liability if a beneficiary waits too long to bring an action. Per Section 1006, a

beneficiary must bring an action alleging a breach of trust no later than one year following the sending of a trustee's report but only if the report informed the beneficiary of the time limit and provided sufficient information so that the beneficiary knew of the claim or reasonably should have inquired into its existence.

Sections 1011 through 1013 address trustee liability to third persons. Perhaps the provision of most interest is Section 1013, which protects a third party in relying on a certification of trust. Section 1011, which is based on a similar provision in the UPC, limits a trustee's personal liability on contracts if the fiduciary capacity was properly disclosed. The trustee is also exempted from personal liability for torts committed in the performance of duties unless the trustee was personally at fault. Section 1012 protects third persons who deal with a trustee in good faith and without knowledge that the trustee is exceeding a power. To receive such protection, however, the third party must have acted in "good faith." Borrowing language from the Uniform Commercial Code, "good faith" is specially defined in Section 1001 to require that the third party follow reasonable standards of fair dealing. The result is better protection for beneficiaries than that provided under the Uniform Trustee Powers Act, under which a third party without actual knowledge of a trustee impropriety was insulated from possible liability no matter how improper or obvious the misconduct.

Article 11
Transitional and Miscellaneous Provisions

Section 1105, which specifies to which trusts the Act will apply, is based on the effective date provision of the Uniform Probate Code. The Act, in general, will apply to trusts already in existence on the date of enactment except to the extent such application would impair a vested right.

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