



Trust Industry Brief

Trust Act 2013: Legislative Updates to the Delaware Code

The Trust Act 2013, which was signed into law by Governor Jack Markell on August 6, 2013, made numerous changes to Title 12 of the Delaware Code, many of which are simply clarifications or codifications of existing Delaware law and only a few of which represent substantive changes or additions. Below is a summary of the most important changes included in the Trust Act 2013.

CLARIFICATIONS AND CODIFICATIONS OF EXISTING DELAWARE LAW

12 Del. C. § 3301 - Expansion of definition of “governing instrument”

Previously, Section 3301(e) defined “governing instrument” as “a will, trust agreement or declaration, court order or other instrument that creates or defines the duties and powers of a fiduciary.” The Trust Act 2013 expanded this definition to include “any instrument that modifies a governing instrument or, in effect, alters the duties and powers of a fiduciary or other terms of a governing instrument.” Thus, the Trust Act 2013 codified the commonly accepted notion that the term “governing instrument” includes not only the original instrument creating the trust but also any judicial or nonjudicial instrument that subsequently modifies the governing instrument or alters the duties or powers of a fiduciary acting thereunder.

12 Del. C. § 3302 – Clarification that trustee has no duty to inquire as to directed trust assets

Section 3302(a) provides that fiduciaries are subjected to a “prudent person” standard of care with respect to the investment of trust assets. Section 3302 (c) further provides that the determination of whether the prudent person standard has been met depends on what the fiduciary knew or should have known about, among other things, the “nature and extent of other investments and resources, whether held in trust or otherwise, available to the beneficiaries.” Section 3302 provides an exception for assets not held by the fiduciary, in which case the fiduciary has no duty to inquire as to their nature and extent. The Trust Act 2013 expanded this exception to include assets that are held by the fiduciary but are subject to the direction of an adviser authorized to direct the fiduciary with respect to investment decisions. Thus, the Trust Act 2013 clarified that, for purposes of satisfying the prudent person standard under Section 3302 with respect to the investment of trust assets, a fiduciary has no duty to inquire as to the nature and extent of investments and resources that are subject to the direction of an investment adviser.

¹ See 12 Del. C. § 3313(d) for a definition of “investment decisions.”



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12 Del. C. § 3303 – Clarification that governing instrument may override any general rule of trust law

Section 3303 (a) provides that the terms of a governing instrument, subject to certain restrictions, may expand, restrict, eliminate or otherwise vary 1) the rights and interests of beneficiaries (including the right to be informed), 2) the grounds for removal of a fiduciary, 3) a fiduciary's duty (if any) to diversify investments and 4) a fiduciary's powers, duties, standard of care, rights of indemnification and liability to beneficiaries. Section 3303 (a) further provides that it is the policy of Section 3303 to give maximum effect to the principle of freedom of disposition and to the enforceability of governing instruments. In furtherance of this policy, the Trust Act 2013 added a new item (5) to Section 3303 (a), which provides that the terms of a governing instrument may expand, restrict, eliminate or otherwise vary "provisions of general application to trusts and trust administration." Thus, the Trust Act 2013 clarified that the terms of the trust instrument, subject to certain limitations, may override any general rule of trust law.

12 Del. C. § 3528 – Clarification that a fiduciary has no duty to exercise statutory decanting power

Subsection (a) of Section 3528 (generally known as the "Delaware Decanting Statute") generally provides that, unless expressly prohibited under the terms of the trust, if a trustee has the authority to invade the principal of the trust to make distributions to, or for the benefit of, one or more beneficiaries, then the trustee may use such authority to distribute principal to a second trust for such beneficiary or beneficiaries. Subsection (e) further provides that, when exercising the authority granted under subsection (a), the trustee (or adviser directing or consenting to the trustee's actions) is held to the same standard of care that is applicable to the trustee when making outright distributions. The Trust Act 2013 clarified existing law regarding when a fiduciary may be held liable for failure to exercise or to consider exercising the fiduciary's statutory decanting power by adding an additional sentence to subsection (e), which provides that no trustee or adviser shall have a duty to exercise the decanting power under subsection (a) and shall not be liable for failure to exercise, or to consider whether to exercise, such power, absent willful misconduct.



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SUBSTANTIVE CHANGES AND ADDITIONS TO DELAWARE LAW

12 Del. C. § 3336 – Provisions for the appointment of successor trustee by trust beneficiaries

The Trust Act 2013 added a new Section 3336 to Title 12, which provides a mechanism for trust beneficiaries to fill a vacancy in trusteeship under certain circumstances. Under the new Section 3336, the trust beneficiaries may appoint a successor trustee by unanimous vote if 1) no trustee is serving (due to death, incapacity or resignation), 2) the governing instrument does not provide an effective means of appointing a successor trustee, and 3) the only remaining dispositive provisions of the trust require the remaining property of the trust to be distributed to one or more beneficiaries (including to another trust of which there is a trustee then serving). For purposes of Section 3336, the beneficiaries entitled to vote are those who are to receive the remaining property of the trust.²

12 Del. C. § 3337 – Barring of claims against revocable trusts

The Trust Act 2013 added a new Section 3337 to Title 12, which codifies existing law by providing that, following the death of the settlor of a revocable trust, claims against the revocable trust are barred to the same extent such claims are barred against the settlor's estate (for example, by reason of the applicable statute of limitations).

12 Del. C. § 3338 - Nonjudicial Settlement Agreements

The most important change included in the Trust Act 2013, from a trust administration perspective, is the addition of a new Section 3338 to Title 12, which authorizes the use of nonjudicial settlement agreements, bringing Delaware in line with the 25 other states (and the District of Columbia) that have adopted a substantially similar provision as part of the Uniform Trust Code (“UTC”).

The new Section 3338 allows “interested persons” to enter into a binding nonjudicial settlement agreement with respect to any matter involving a trust (other than a charitable or noncharitable purpose trust described in Section 3541 of Title 12), provided that the agreement does not violate a “material purpose of the trust” and “includes terms and conditions that could be properly approved by the Court of Chancery.”

² In the case of assets distributable to another trust, then the trustee of that trust shall be entitled to vote.



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12 Del. C § 3338 - Nonjudicial Settlement Agreements (cont..)

Subsection (a) defines an “interested person” as any person whose consent would be required for a consent petition in the Court of Chancery. Rule 101 of the Court of Chancery Rules provides that a consent petition, and therefore, a nonjudicial settlement agreement, must include consents from (at a minimum) 1) trustees and other fiduciaries, 2) trust beneficiaries (generally those with a present interest in the trust and those whose interest in the trust would vest if the present interest in the trust terminated), 3) the trustor of the trust, if living, and 4) all other persons having an interest in the trust according to the express terms of the trust instrument, including holders of powers and persons having other rights, held in a nonfiduciary capacity, relating³ to trust property.

Subsection (d) provides a list of seven matters that may be resolved by nonjudicial settlement agreement. These include 1) the interpretation or construction of trust terms, 2) the approval of a trustee’s report or accounting, 3) the direction to a trustee to refrain from performing a particular act or the grant to a trustee of a particular power, 4) the resignation or appointment of a trustee, 5) the determination of a trustee’s compensation, 6) the transfer of a trust’s principal place of administration; and 7) the liability of a trustee for an action relating to the trust.

According to the Comments to UTC Section 111, upon which Section 3338 is based, subsection (d) is a nonexclusive list of matters that may be resolved by agreement. Thus, nonjudicial settlement agreements under Section 3338 may be used to resolve any trust matter, provided that the agreement does not violate a material purpose of the trust and contains terms and conditions that could properly be approved by the Court of Chancery. Unfortunately, neither Section 3338 nor UTC Section 111 (or the Comments thereto) provide a definition of “material purpose.” Whether an agreement violates a material purpose of the trust must be determined on a case-by-case basis and generally depends on the underlying intentions or objectives of the settlor in establishing the trust.

³ Note that the Delaware Virtual Representation Statute (12 Del. C. § 3547, discussed below) applies to nonjudicial settlement agreements. Therefore, a nonjudicial settlement agreement may still be effective without the consent of any one or more of the above-listed interested persons if such interested person is effectively represented and bound by another person pursuant to Section 3547.



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12 Del. C § 3338 - Nonjudicial Settlement Agreements (cont..)

Subsection (e) of the new Section 3338 provides that any interested person may bring a proceeding in the Court of Chancery to interpret, apply, enforce or determine the validity of a nonjudicial settlement agreement, including determining whether the representation under Section 3547 was adequate. This provision expands on Section 111 of the UTC, which provides only that an interested person may request the court to approve a nonjudicial settlement agreement, to determine whether the representation was adequate, or to determine whether the agreement contains terms and conditions the court could have properly approved.

12 Del. C. § 3547 – Creation of presumption of material conflict of interest for virtual representation purposes

Section 3547 (generally known as the “Delaware Virtual Representation Statute”) provides that, with respect to any judicial proceeding or nonjudicial matter, certain minor, unborn, incapacitated, unknown, unascertainable and contingent successor remainder beneficiaries may be represented and bound by another person, provided that both parties have “substantially identical” interests and there is no “material conflict of interest” between the parties with respect to the particular question or dispute at hand.

In an attempt to clarify the circumstances under which virtual representation may be disallowed due to a conflict of interest, the Trust Act 2013 added a new subsection (e) to Section 3547, which provides that a material conflict of interest will be presumed to exist when:

- 1) The representative, as a result of the matter at hand, would be appointed to a fiduciary or non-fiduciary role relating to the trust, unless the representative already serves in such a role and would not receive greater authority, broader discretion or increased protection by reason of the new appointment;
- 2) The representative serves in a fiduciary or non-fiduciary role relating to the trust and, as a result of the matter at hand, would receive greater authority, broader discretion or increased protection; and



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12 Del. C § 3547 – Clarification of when a material conflict of interest exists for virtual representation purposes: (cont..)

- 3) There is any other actual or potential conflict of interest with respect to the particular question or dispute, including conflict resulting from a different investment horizon or an interest in present income over growth capital (i.e., the interests of current income beneficiaries over remainder beneficiaries).

This language mirrors similar language included in the recent amendments to Rule 100 of the Court of Chancery Rules (pertaining to matters that must be addressed with particularity in each consent petition).

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